Builders' Liens:

Towards Greater Assurance of Payment

Preliminary Report of the
Joint Government/Industry
Task Force on Builders' Liens

September 1988

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Message from the Chairman

The Joint Government/Industry Task Force on Builders' Liens has been meeting regularly since September, 1987. It received representations from industry associations, professional associations, corporations and individuals and has carefully considered them all. As well, the Task Force received briefings on builders' lien law and procedures from experts familiar with the legislation in Ontario, Saskatchewan and California.

The Preliminary Report deals primarily with principles. Since some are novel, it is expected that they will stimulate significant discussion. In the view of the Task Force, these principles, if adopted in legislation, will provide greater assurance that those in the construction and energy industries with lien rights will be paid. They will not, however, guarantee that result. Where an owner walks away from a project, or a contractor or subcontractor underbids a job, or a contractor or subcontractor is dishonest and unscrupulous, legislation cannot provide a fail-safe guarantee that those who provided work or supplied materials will be paid.

Although it was initially anticipated that there would be competing interests represented on the Task Force which could not be easily reconciled, such was not the case. Most of the recommendations contained in this Preliminary Report are made unanimously. Although there were reservations by one or two members on some isolated issues, no member of the Task Force expressed strong opposition to any of those recommendations.

The Task Force welcomes further input on its Preliminary Report from any interested group or member of the general public and will consider all written submissions received prior to November 15, 1988. It is the intention of the Task Force to submit a Final Report with draft legislation to the Attorney General in time for the Spring 1989 Session of the Legislative Assembly.

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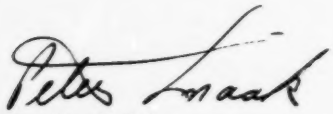

Peter Knaak, Q.C.,
Chairman

Chapter 1: Introduction

I. Joint Government/Industry Task Force on Builders' Liens

1. Establishment:

The Joint Government/Industry Task Force on Builders' Liens was established by Ministerial Order of the Attorney General (M.O. 5/87 dated June 18, 1987). The government's intention to form such a Task Force was announced in the Speech from the Throne on March 5, 1987.

A motivating factor behind the existence and composition of the Task Force was to permit the industries directly affected by the Builders' Lien Act to develop recommendations for a solution to the problems which they faced with respect to the legislation.

2. Membership:

The Task Force consists of representatives nominated by a number of associations which have a direct interest in the Builders' Lien Act. A list of the members of the Task Force and the associations which nominated them is attached as Schedule "A".

The Chairman, Peter Knaak, Q.C., was appointed by the Attorney General. Mr. Knaak is a senior member of the Alberta Bar and has extensive experience in all aspects of corporate and commercial law.

3. Mandate of the Task Force:

The Ministerial Order of the Attorney General establishing the Task Force set out its terms of reference in the following manner:

"(a) to review the Builders' Lien Act;

(b) to consider the views of those interested persons and groups who make submissions to the Task Force;

(c) to examine alternatives to the Builders' Lien Act; and

(d) to prepare draft legislation implementing the findings and recommendations of the Task Force."

4. Method of Operation:

The Task Force had four main sources of information. First, the Task Force members themselves have diverse experience with the Builders' Lien Act and represent a substantial source of expertise. Second, the Task Force met with three persons considered expert in the field of builders' lien legislation from three different jurisdictions: Kevin McGuinness who acted as Secretary to the Attorney General's Advisory Committee in Ontario which reported in April 1982; Gary G.W. Semenchuck, Q.C., who was Chairman of the Special Advisory Committee to the Minister of Justice on Builders' Liens in Saskatchewan which reported in August 1984; and James Drummond from the San Diego, California law firm of Hillyer and Irwin who is a noted practitioner and lecturer on lien law in the State of California. As well, the Task Force advertised publicly and corresponded with virtually all groups and associations which might have an interest in the Builders' Lien Act, inviting them to make written representation to the Task Force. All those who made such representations were invited to discuss them with the Task Force, as well as to discuss certain preliminary views which the Task Force had developed itself.

Lastly, the Task Force benefited from the following reports on builders' lien law reform:

(a) Report of the Honourable Harold Francis Thomson, Q.C., Commissioner (Saskatchewan 1963) (referred to as the "Thomson Report");

(b) Report of Ontario Law Reform Commission, "The Mechanics' Lien Act", (Ontario 1966) (referred to as the "OLRC Report");

(c) Report of His Honour Chief Judge Neiles V. Buchanan (Retired) (Alberta 1967) (referred to as the "Buchanan Report");

(d) Law Reform Commission of British Columbia, "Report on Debtor Creditor Relationships: Part II - Mechanics' Lien Act: Improvements on Land" (British Columbia 1972) (referred to as the "British Columbia Report");

(e) Report to the Attorney General of the Nova Scotia Law Reform Advisory Commission on Builders' Liens (Nova Scotia 1976) (referred to as the "Nova Scotia Report");

(f) Institute of Law Research and Reform, Report No. 30 "The Builders' Lien Act: Certain Specific Problems" (Alberta 1979) (referred to as the "Institute Report");

(g) Manitoba Law Reform Commission "Mechanics' Liens Legislation in Manitoba" (Manitoba 1979) (referred to as the "Manitoba Report");

(h) Report of the Attorney General's Advisory Committee on the Draft Construction Lien Act (Ontario 1982) (referred to as the "Ontario Report");

(i) Special Advisory Committee to the Minister of Justice on Builders' Liens, "Liens in the Construction Industry" (Saskatchewan 1984) (referred to as the "Saskatchewan Report").

During the course of its deliberations, the Task Force referred to the following legislation as amended:

(a) Ontario: Construction Lien Act, 1983, S.O. 1983, c. 6;

(b) Manitoba: The Builders' Liens Act, S.M. 1980-81, c. 7;

(c) Saskatchewan: The Builders' Lien Act, S.S. 1984-85-86, c. B-7.1;

(d) British Columbia: Builders Lien Act, R.S.B.C. 1979, c. 40; and

(e) Alberta: Builders' Lien Act, R.S.A. 1980, c. B-12.

II. Legislative History of the Builders' Lien Act

Since it was first enacted in Alberta in 1906 [S.A. 1906, c. 21, s. 42 repealed the Mechanics' Lien Ordinance of the North-West Territories, R.O. 1888, c. 48; C.O. 1898, c. 59], the Builders' Lien Act has been amended, consolidated and re-enacted 30 times. A detailed legislative history is attached to this report as Schedule "B". As the British Columbia Report put it in considering its own legislation:

> "One might be forgiven for thinking that by now, 90 years and 31 amendments later, the Act ought to have reached at least a state of satisfactoriness. Nothing could be further from the truth. Suggestions for change are frequent. Complaints concerning the operation of the Act are legion. The Act has been and continues to be a constant source of difficulty and irritation for those engaged in the construction industry and for their advisors." (at page 8)

As can be seen by Schedule "B", the same state of affairs appears to be the case in Alberta. One need only compare the size and complexity of the construction industry today with that in the early days of builders' lien legislation to understand the constantly changing nature of the legislation. As the Buchanan Report noted:

> "[The Mechanics' Lien Act] is an Act the basic pattern of which was set in the horse and buggy days: by patch work additions and subtractions, an attempt has been made to adapt its provisions to the days of multi-million dollar construction, and without marked success." (at page 16)

The Buchanan Report rejected the suggestion that the Act should contain trust provisions. It recommended not only that there should be no extension of the then 35 day period within which to register liens, but also that the 120 day registration period provided for the oil and gas industry should be reduced to 35 days in order for there to be uniformity. As well, the Buchanan Report recommended that the priorities between mortgagees and lienholders should be reversed and tied to registration as that "would avoid trespass upon the Torrens system of land registration so highly esteemed by courts and lawyers...". (at page 69). The Buchanan Report resulted in a new piece of legislation called The Builders' Lien Act, S.A. 1970, c. 14.

The report of the Institute of Law Research and Reform dealt with a number of specific problems which practitioners had brought to the Institute's attention and which were causing problems in practice. The most important recommendations of the Institute were intended to allow statutory holdbacks to be paid out upon substantial completion of a contract or subcontract. Shortly after that report was published, the Alberta Construction Association made an extensive submission based on the Institute's recommendations and incorporating its own recommendations as well. The Institute Report and the submission of the Alberta Construction Association were reviewed by a committee of lawyers in 1984 and 1985, the result of which was the Builders' Lien Amendment Act, 1985, S.A. 1985, c. 14.

The amending legislation clarified many of the problems dealing with the release of the holdback upon substantial completion. It provided a procedure by which a contractor or subcontractor could issue his own certificate of substantial completion which started the registration period running in order to allow a partial release of holdback. It also imposed a trust upon the money paid under a certificate of substantial completion as it flowed from level to level. As well, the amending legislation increased the lien period to 45 days. However, the amendments did nothing to simplify the complexity of the legislation.

III. Repeal of the Builders' Lien Act

Although not part of its mandate, the Buchanan Report suggested that consideration might be given to repealing the Act:

> "The information available to me from many sources outside as well as inside the Province suggests that repeal of the Mechanics' Lien Act would have a generally beneficial effect on the building industry... As legislation which confers special benefits on particular classes of persons, the Act is justified only if there is an important reason for conferring such privileges. The evidence before me has not indicated a pressing need for such protection." (at pages 47 and 48)

The Institute Report stated that there was "strong support on our Board for [repeal]" but that before "considering a recommendation for repeal, however, we would have to conduct our own study to assess the effects of the Act and the likely effects of its repeal." (at page 2). Because of other work, the Institute was not able to undertake that assessment.

The British Columbia Report identified five main arguments in favour of repeal:

1. The Act slows down the flow of funds along the construction chain;

2. It induces a false sense of security;

3. It gives rise to technical difficulties;

4. It is an instrument of blackmail; and

5. It is unjust. (at pages 20-3)

The Manitoba Report commented on these arguments:

> "The last argument [i.e., it is unjust] is probably the strongest because it is founded on an attack against the fundamental rationale for the existence of the legislation. The argument is that the Act gives a special protection to a particular class of people, namely people in the construction industry, as distinguished from other creditors. The answer to this argument offered by the Law Reform Commission of British Columbia was that the special circumstances of the construction industry warrant this special protection." (at page 13)

Neither the British Columbia nor the Manitoba Report recommended repeal of the legislation.

Since lien rights are an historically accepted part of the construction and energy industries in every common law province as well as in virtually every State of the Union, the Task Force was unanimous in its recommendation not to recommend repeal of the Act.

IV. The California System

The emphasis of Canadian lien legislation is on legal sanctions and the legal enforcement of rights which in turn rely on the judicial process. However, other than the threat of a lien claim or the threat of a breach of trust action, there is no mechanism to ensure that payment in the construction or energy industries is occurring. The enforcement of rights involving the judicial process is complex and expensive. If the "threat" is not effective, the actual remedy is not only time consuming but also very expensive and therefore likely to be cost-inefficient.

The California system uses a different mechanism to ensure payment. It relies less on the threat of legal sanctions, preferring to rely on lien waivers to make sure that payment flows down the construction pyramid. In California, the lien law makes the owner liable for all liens filed with no limitation. The law also provides for lien waiver forms. All persons working on the project must notify the owner, construction lender and contractor that they are working on the project in order to have rights under the legislation. The owner will make the first advance but will only make the second advance if everyone in the pyramid has been paid as evidenced by the lien waiver forms. If some waivers are not received, the owner will hold back those funds from the contractor. This process, through conduct of the owner, assures that everyone in the construction pyramid is paid so long as the owner does not default.

As well, licensing of contractors and subcontractors exists which imposes payment requirements which, if breached, may result in the loss of the licence.

The California system is appealing because, in most cases, it prevents a problem from developing, and, as a result, the complex and cost-inefficient legal enforcement systems of the Canadian legislation would need to be relied upon less. Nevertheless, many large projects in Canada already function much like the California system in that the owner on a large project will generally get assurance that everyone in the construction pyramid has been paid prior to releasing the next advance. This system of further payment only upon receipt of previous payments is not unlike the California lien waiver system.

The Task Force recommends that statutory forms should be provided that will serve as evidence of payment receipt such that an owner can be assured that there will be no liens arising as a result of work for which a receipt has been issued.

Since the construction sector in Alberta is relatively small compared to that in California, and given that Canada has already developed a jurisprudence in relation to trusts and other elements of the present lien legislative framework, the Task Force is of the opinion that an attempt should be made to make the Alberta model more effective before considering a scheme similar in all respects to the California scheme for the construction and energy industries in this province.

V. Objectives of the Builders' Lien Act

During 1985 and 1986, the Attorney General and the Minister of Public Works received submissions from the Alberta Construction Association urging the government to review the Builders' Lien Act. There was a growing indication in the construction and energy industries that contractors, subcontractors and suppliers were not being paid. The blame, mistakenly or not, was increasingly focused on the Builders' Lien Act.

It was noted by the Task Force that Alberta suffered a serious recession from 1982 to 1986 in general, and particularly in the construction and energy industries. The downturn in those sectors during those years saw an unusually large number of owners, contractors and subcontractors suffering insolvency or bankruptcy. As a result, greater reliance than usual was placed on the Builders' Lien Act as a collection vehicle.

Early in its deliberations, the Task Force resolved that the primary objective of its proposals would be to create a legislative framework which would provide greater assurance that everyone in the construction and oil and gas industries would be paid. As the Task Force reviewed lien legislation in other jurisdictions and assessed how these other jurisdictions achieved their objectives, it became clear that "lien" legislation, as it is named in those provinces with statutory trust provisions, is much more than merely "lien" legislation. The addition of comprehensive trust provisions has transformed this legislation into a virtual payment assurance scheme for the construction and energy industries.

The imposition of a statutory trust on the contractual chain of payment completely alters the way in which the individual links along the chain may deal with contractual money coming into their hands. The imposition of a statutory trust creates a statutory obligation to pay those who are owed money, that is, the "beneficiaries" of the trust, for the breach of which serious criminal and civil penalties may ensue including the personal liability of directors and officers of a corporate trustee. However, where an owner walks away from a project, or a contractor or a subcontractor underbids a job, or a contractor or subcontractor is dishonest and unscrupulous, it is the view of the Task Force that neither the lien nor the trust can provide a fail-safe guarantee that those who provided work or furnished materials to the project will be paid.

The Task Force was of the view that any proposed changes to the legislation should not be skewed to the most severe economic circumstances, since considerable time and expense is involved in adhering to the legislation and enforcing rights under it. Although the Task Force felt that the legislation should be drafted to accommodate a more stable economic environment, it also felt that it should be more equitable and more effective during a period of recession.

VI. Problems with the Existing Legislation

The present Builders' Lien Act was assessed in relation to its ability to deal with the main concerns expressed to the Task Force, both by the members of the Task Force themselves and by those persons who made representations to it. Those concerns may be summarized as follows:

1. One of the most often expressed complaints was simply that "I didn't get paid." There appeared to be a number of reasons for this result, namely:

   (a) In situations where the contractor became insolvent, or was on the verge of insolvency, his banker may have seized any available cash in his account which might otherwise have been available for payment to subcontractors and suppliers. The same scenario may be applied to subcontractors in relation to their subcontractors and suppliers;

   (b) Contractors or subcontractors may have been using cash flow from a current project to pay off debts incurred on prior projects or to pay debts unrelated to any construction;

   (c) An unscrupulous contractor or subcontractor may have "scooped" the money, thus making his company insolvent. Such a contractor or subcontractor may merely start over with a new corporate entity and repeat the cycle; and

   (d) If the owner became insolvent, the lender, who generally has priority for principal and interest over lien claimants, foreclosed the interests of the owner and, in most cases, all lien claimants. Thus, the lien claimants were left without money or an effective remedy.

2. The Alberta Construction Association and others made a strong case that the 15 percent mandatory holdback creates a significant impediment to the cash flow in the construction pyramid and that such restriction in cash flow itself creates insolvencies and other business difficulties.

3. The Task Force obtained a report and prepared a statistical analysis of all liens filed in Alberta in 1986. It appeared that the majority of such liens were for under $5,000. The complexity of the legal process and the associated legal costs of enforcing liens virtually eliminates any benefit to the lien claimant if his claim is under $5,000. As the Construction Law Subsection (Southern) of the Canadian Bar Association observed in its submission to the Task Force:

> "One of the problems with the procedure for dealing with builders' liens under current Builders' Liens legislation is that the cost of resolving smaller lien claims is prohibitive given the complicated and time consuming court applications and attendant cross examinations on affidavits, production of documents and examinations for discovery." (at page 5)

4. Many people, including professionals who deal frequently with the legislation, pointed out to the Task Force that the current Builders' Lien Act is extremely complex and difficult to understand.

5. The Task Force heard the opinion that the Builders' Lien Act encourages unwarranted reliance on what appears to be the "security" created by the legislation and that such reliance encourages bad business practices. If the "holdback" needed to be relied upon for ultimate payment, generally very little remained for lien claimants after pro rata distribution and the associated legal costs in enforcing lien rights.

6. Many people expressed the view that they were unwilling to register a lien because of the risk of being "blacklisted" which would seriously jeopardize their future job opportunities in the industry.

7. There appears to be a lack of elementary knowledge by some owners and subcontractors of their rights and obligations under the legislation.

8. The Task Force, which includes representation from the oil and gas industry, was made aware of various problems which that industry faces with the current legislation. It was pointed out that the Builders' Lien Act might need special consideration to meet the needs of the industry. For example, it was strongly urged that, while 45 days may be an appropriate time within which to register a builders' lien in the construction industry, because of the nature of payment practices in the oil and gas industry, 90 to 120 days would be more appropriate for it.

VII. Summary of Recommendations

Throughout this report, it is more useful to think of the Task Force's recommendations in terms of a scheme to provide greater assurance of payment for the construction and energy industries, since that provides a better framework for discussion and assessment of those recommendations and the objectives which the Task Force is attempting to achieve.

The main recommendations of the Task Force may be summarized as follows:

1. Implementation of comprehensive trust provisions;

2. A requirement that the trustee maintain a consolidated trust account for all trust funds;

3. Implementation of a new remedy called a "Stop Notice" such that the remedy to pursue trust funds would be separate from, and independent of, the remedy to encumber land;

4. Elimination of the statutory holdback;

5. Institution of a registration requirement for all contractors and subcontractors in both the construction and the oil and gas industries who, in the normal course of business, handle trust funds;

6. An increase in the lien period for the oil and gas industry to 90 days; and

7. The Crown should be bound by the Builders' Lien Act.

Although there are a number of other recommendations, the scheme of the new legislation will be based on the above principles. All recommendations and the reasons for them are detailed in the report that follows. However, it should be noted that the Task Force does not propose any change in the present ability of contractors, subcontractors and suppliers to register builders' liens.

One of the surprising elements of the Task Force's deliberations was the virtual unanimity of agreement with respect to the recommendations being made in this report. Although it was initially anticipated that there would be competing interests which might be difficult to reconcile, such was not the case.

Chapter 2: The Statutory Trust

I. Introduction

The Task Force recommends that comprehensive trust provisions should be imposed by statute on owners, contractors and subcontractors in the construction and oil and gas industries. The details of those trust provisions and the logic behind them are the subject of this chapter.

II. Concept of the Trust

Trust law is based on the proposition that if A pays money to B "in trust for C," B may not use that money for any other purpose than paying C. Conceptually, the imposition of a trust, whether by statute, contract or operation of law, alters what would otherwise be a debtor-creditor relationship.

According to the law of contract, once a person receives a sum of money, he acquires the legal and beneficial title to that money. He is not bound to hold it for any particular purpose, but may dispose of it as he wishes. However, with the statutory imposition of a trust, in the context of the construction and oil and gas industries, all money received on account of the contract price is held in trust for the benefit of, and can only be applied to payments owed to, those to whom trust obligations exist. Only when all such accounts have been paid may the contractor or subcontractor take his profit. In other words, the person who is the trustee of the trust fund only acquires a beneficial interest in money that exceeds all his trust claims.

Thus, the logic of a trust in the construction and oil and gas industries is simple. It is to prevent funds, paid by the owner for the construction of an improvement, being diverted either to pay creditors of a different improvement or to pay the bank for previously incurred debts. The ultimate goal of the trust is to ensure that funds arising out of a specific project are used to pay for work and materials supplied to it.

In summary, the trust creates a structure which requires funds to flow from the owner to the contractor to subcontractors and so on until the last beneficiary has been paid. If the funds do not flow, there is potentially a breach of trust, which could ultimately result in criminal and civil liability for one or more directors and officers of a corporate trustee.

III. History of Trusts in the Construction and Energy Industries

The statutory imposition of a trust upon construction industry contracts is of fairly recent origin. It was first introduced in Manitoba in 1932. Ontario adopted its equivalent in 1942 and British Columbia did the same in 1948. When a new act was introduced in Saskatchewan in 1973, it included trusts for the first time. In **Minneapolis-Honeywell Regulator Company Limited v. Empire Brass Manufacturing Company Limited**, [1955] S.C.R. 694, 3 D.L.R. 561, Mr. Justice Rand explained the rationale for trust provisions, commenting on the British Columbia legislation, in the following manner:

> "The Act is designed to give security to persons doing work or furnishing materials in making an improvement on land. Speaking generally, the earlier sections give to such persons a lien on the land, but that is limited to the amount of money owing by the owner to the contractor under the contract when the notice of the lien is given to him: only thereafter does he pay the contractor at any risk.
>
> For obvious reasons this is but a partial security; too often the contract price has been paid in full and the security of the land is gone. It is to meet that situation that s. 19 has been added. The contractor and subcontractor are made trustees of the contract moneys and the trust continues while employees, material men or others remain unpaid." (S.C.R. at page 696)

Alberta has never had comprehensive trust provisions. The Buchanan Report recommended against them for the following reasons:

> 1. "The trust clauses have little significance for the large and generously financed corporations, whether contractors or subcontractors. They keep excellent records; for each contract separate accounts are maintained and funds from various jobs are either not intermingled or can readily be accounted for. With adequate funds at their disposal there is no need or temptation to apply contract funds to any purpose forbidden by the trust clause.";
>
> 2. "The presence of the trust clause in the Act is a threat, and possibly a deterrent to the misapplication of funds, only to the underfinanced or to the dishonest."; and
>
> 3. "The assignment of contract funds has long been the choice security used by contractors in securing interim financing from banks, pending the receipt of draws from lenders secured by mortgage." (at pages 23, 24 and 27)

In the 1985 amendments to the Builders' Lien Act, a trust was introduced in the following terms:

"16.1(1) Where

(a) a certificate of substantial performance is issued, and

(b) a payment is made by the owner after a certificate of substantial performance is issued

the person who receives the payment, to the extent that he owes money to persons who provided work or furnished materials for the work or materials in respect of which the certificate was issued, holds that money in trust for the benefit of those persons."

As substantial performance of a contract does not generally occur until it is 97 percent completed, this trust is limited to a very small percentage of the project funds.

IV. Remedies of a Trust Beneficiary

The remedies of a trust beneficiary, unlike a mere creditor, are either in personam or in rem; that is, he may either sue in damages for breach of trust or sue to recover the trust property itself. A mere creditor, on the other hand, is limited to suing for damages for breach of contract.

It is intended that officers, directors and agents of a corporate trustee, who consent to the diversion of trust funds, will be personally liable, even if those funds were expended for proper corporate purposes. This is an extremely valuable extension of liability since the personal action runs into none of the difficulties involved with tracing.

Generally, a beneficiary of a trust may follow the trust property, that is, "all money received by an owner, a contractor or a subcontractor, on account of the contract price", into the hands of a person who received it with knowledge of its source and notice that the payment was a breach of the trustee's duties. As the Supreme Court of Canada put it in 1896:

> "A great number of cases decided in courts of equity ranging over more than a century have established that trust moneys may always be traced into property of any species into which it may have converted, in such a way that the court will give this *cestui que trust* as nearly as possible the same interest in the property as that which he had in the money of which it is the produce." (**Carter v. Long & Bisby**, 26 S.C.R. 430 at 432 per Sir Henry Strong, C.J.)

Lastly, another feature of the law which distinguishes the rights of a trust beneficiary from those of a mere creditor is that in the event of a trustee's bankruptcy, the beneficiary of the trust may claim the identifiable trust funds as his own property and not subject to the bankrupt's liabilities. A trust beneficiary therefore has an advantage over unsecured creditors in a trustee's bankruptcy in that he can take his property from the bankrupt's assets on the basis that it never was the trustee's property and should not therefore be subject to the bankruptcy.

V. Objectives of the Trust in the Construction and Energy Industries

The trust will potentially solve a number of problems which were identified to the Task Force. Virtually every submission to the Task Force urged adoption of the trust. While the general objective of the trust is to make sure that everyone who works on the job gets paid, there are two situations which cause many of the difficulties in the construction and oil and gas industries which the trust attempts to remedy. The first is the situation in which a contractor or a subcontractor settles past accounts with current funds. The second is the situation in which a bank uses money in a contractor's or subcontractor's account to reduce his indebtedness to the bank, which indebtedness may have arisen out of matters unrelated to the working capital needs of the current project. Each of these will be dealt with in turn.

1. Settling Past Accounts with Current Funds:

Many of the problems in the construction and oil and gas industries occur on seriously underfinanced projects. These problems are magnified in a poor economy such as Alberta experienced in the early 1980s.

On such projects and in such times, there is a natural tendency to pay debts on past jobs with funds being earned on a current one. When insolvency occurs, subcontractors and suppliers on the current project are left with unpaid bills and, if the owner has fulfilled his contractual and statutory obligations, find themselves with little or no chance of recovering on a lien claim.

The trust attempts to prevent this situation from occurring by making it a breach of trust for a contractor or subcontractor to use contract money for any other purpose than settling current accounts arising on a current project. That is, trust restrictions do not allow the contractor or subcontractor to use his receipts on the principal project to solve liquidity problems on other projects until all his trust obligations on the principal project are satisfied.

A breach of trust is an offence under the Criminal Code which can be accompanied by severe penalties. The civil liability of a trustee is to compensate the beneficiary for any loss suffered as a result of a breach of trust.

Neither the case law nor more recent statute law show any hesitation in piercing the corporate veil in order to impose personal liability on officers and directors of a company for their company's breach of trust.

Obviously, the combination of these penalties forms a strong deterrent to the commission of a breach of trust.

2. A Bank's Use of Trust Funds to Reduce Indebtedness Not Incurred to Pay Beneficiaries:

At the present time, there is no legal impediment in Alberta to accounts receivable being pledged as security for interim financing from banks. However, the statutory imposition of a trust will mean that contractors will only be able to use the assignment of contract funds as security for a loan if the loan proceeds are used to pay beneficiaries. As Callaghan, A.C.J., of the Ontario High Court so succinctly put it in **First City Capital Ltd. v. Petrosar Ltd.**, 61 O.R. (2d) 193

> " 'You cannot assign what you do not have.' This is a fundamental maxim of the law of assignments." (at page 195)

In other words, the statutory imposition of a trust will prevent banks from taking trust funds, which should have been used to pay subcontractors and suppliers, unless the bank advanced funds for the specific purpose of paying those beneficiaries. If the bank has advanced funds which have been used to pay subcontractors and suppliers, there is no question that a bank may repay itself from money that would otherwise be trust funds. Both the Ontario and Saskatchewan legislation provide that a contractor may retain funds that were borrowed in order to pay subcontractors and suppliers. In other words, such money never becomes part of the trust. The Task Force's recommendations include this provision as well.

With respect to a bank's liability for breach of trust for taking a trustee's receivables to repay itself, the cases turn on whether or not the bank knew, ought to have known, or at least was put on inquiry, that the funds being used to pay down the line of credit were trust funds: see **Westex Manufacturing Ltd. v. Wilson et al**, 21 C.L.R. 133 (B.C.S.C.) and **Heating Engineering Installations (1981) Ltd. et al v. Raymond Contractors Ltd. et al**, 56 Sask.R. 119, 24 C.L.R. 264 (Sask.Q.B.).

Elsewhere in this report, the Task Force recommends that contractors and subcontractors should be required to establish a separate consolidated trust account for trust funds. This will differentiate more clearly between general funds, which can be assigned, and trust funds, which cannot.

VI. Discussion of the Task Force's Recommendations

1. Relationship between a Trust Beneficiary and a Lien Claimant:

In the Task Force's view, the lien is separate from, and independent of, the trust. That is, one need not have registered a lien to be considered a beneficiary of the trust. However, for a person to be a beneficiary of a trust, one must have been entitled at some time to a builders' lien.

Elsewhere in this report, the Task Force recommends that an owner should be a trustee for any funds derived from a bona fide sale of the improvement, by the owner, subject to prior encumbrances and normal expenses. Thus, where the owner's land is sold in a lien action, lien claimants, being holders of prior registered encumbrances, will have priority over all other beneficiaries.

In those cases where a lien is registered and the owner's land is not sold, the Task Force is of the opinion that there should be no priority in the distribution of trust funds between lien claimants and those who have served Stop Notices.

Lastly, the Task Force agrees with the Saskatchewan Report that the

> "expiry of the lien period should not affect a trust beneficiary's right to assert his claim against the trustee or a third party acting in breach of the trust nor should it create a priority among trust beneficiaries." (at page 41)

2. To Whom is a Trust Duty Owed?

The Task Force unanimously agreed that initially there must be a contractual relationship between the trustee and the beneficiary before a trust obligation will arise. This is the view which has been adopted in both Ontario and Saskatchewan.

However, this limitation of a contractual relationship can be overcome by the Stop Notice provision which the Task Force is recommending. If a person, other than the contractor, serves a Stop Notice on the owner, then the owner will be impressed with trust obligations to the person serving the Stop Notice for the amount claimed in it. In other words, the service of a Stop Notice on the owner by a subcontractor or a supplier makes the owner not only a trustee to the contractor, with whom he has a contractual relationship, but also to the person who has served the Stop Notice, with whom he does not have a contractual relationship, for the amount claimed in it. The Stop Notice is discussed in chapter 3 of this report.

3. Termination of the Trust:

The trust should be terminated and the trustee discharged of trust obligations upon payment of the amount owed to the beneficiary, and where a Stop Notice is served, upon setting aside the amount claimed in it. The duty of each trustee, whether a contractor or a subcontractor, is simply to pay what he receives from the project to those he owes in relation to that project. Once payment is made of the total trust funds, the trust is terminated. In other words, only those funds received by a trustee on account of the improvement are trust funds and no sum larger than that. Upon payment of that amount, subject to setoffs arising out of the improvement, the trust obligation is fulfilled and the trust is completed.

4. Consolidated Trust Account:

Legislation in the provinces which have imposed trusts has never required those trust funds to be kept in a separate trust account. In the view of the Task Force, this has become a serious deficiency because of recent cases in which banks sometimes are held entitled to funds which should have been used to pay subcontractors and suppliers.

It seems logically consistent to the Task Force to impose a statutory requirement to keep trust funds separate and apart from the general revenue of a contractor or a subcontractor. If trust funds can be commingled with general revenues, the trust provisions will not ensure that any funds will remain in the contractor's bank account when insolvency occurs. It is more likely that a contractor with a tight cash flow will spend every cent he receives. Thus, to allow the commingling of trust funds and general revenue is to invite the very occurrence which the Task Force is trying to prevent, namely, a breach of trust.

Therefore, the Task Force recommends that contractors and subcontractors should be statutorily required to maintain, in Alberta, a consolidated trust account for funds arising on contracts under which liens may arise. However, the obligation to maintain a separate trust account should not apply to an owner. Since the contractor has a lien against the owner's interest to prevent the owner's unjust enrichment, there is no necessity for an owner to maintain a separate trust account. Further, where the mortgagee is financing the improvement, generally the money will pass from the mortgage company into a lawyer's trust account so the owner never has possession of trust funds. As well, such an obligation for the owner would be impractical. However, an operator on an oil and gas project, who would have the trust obligations of an owner according to the Task Force's recommendations, should be required to maintain a separate consolidated trust account.

5. The Owner's Trust Funds:

The imposition of a statutory trust in effect creates a statutory obligation on the trustee to pay those who are owed trust money. The breach of that obligation carries with it serious criminal and civil penalties including the personal liability of directors and officers of a corporate trustee. Therefore, it is essential to identify those funds which form the trust property in order to know which money carries with it trust obligations.

In the view of the Task Force, the owner should be a trustee for the following funds:

(a) Funds secured by a mortgage or other security and advanced to the owner for the purpose of financing the improvement. Both the Ontario legislation and the Saskatchewan legislation provide that all amounts received by an owner that are to be used in the financing of the improvement, including any amount that is to be used in the payment of the purchase price of the land and the payment of prior encumbrances, constitute, subject to the payment of the purchase price of the land and prior encumbrances, a trust fund for the benefit of the contractor;

(b) Any funds in the hands of the owner, or received by the owner, for payment of the improvement;

(c) Any funds, or source of funds, identified by the owner to the contractor as being funds earmarked for paying the costs of the improvement. The identification of trust funds of the owner is relatively easy if the funds are borrowed and advanced by the lender or are derived from the improved land. It is more difficult, however, to identify funds that the owner has "set aside" for purposes of financing the project. It is proposed, therefore, that if an owner represents to a contractor funds, or a source of funds, that he will use to finance the project, those funds will become trust funds as well. For example, if the owner has identified to the contractor that the proceeds are to come from the sale of another property, the sale proceeds of the other property would be trust funds in the event that the contractor has not been paid the full amount due and owing to him under the contract;

(d) Any revenue generated from the improved land, subject to prior encumbrances;

(e) Any funds derived from a bona fide sale of the improvement by the owner, subject to prior encumbrances and normal expenses; and

(f) The net proceeds from insurance should the improvement be damaged or destroyed.

6. Setoff:

A trustee may set off against trust funds any counterclaim that he has against a beneficiary arising out of the project. In **United Metal Fabricators Ltd. v. Voth Bros. Construction (1974) Ltd. et al**, 42 D.L.R. (4th) 193, 20 B.C.L.R. (2d) 274 (B.C.C.A.), Mr. Justice Taggart held that the relevant section of the B.C. legislation

> "contemplates the trust attaching only to moneys due 'for work done or materials supplied on the contract'. That must mean work properly done as contemplated by the contract between the parties. In effect, it is any net amount due by the contractor to the subcontractor which constitutes the *corpus* of the trust." (D.L.R. at page 200)

The Ontario legislation permits the trustee to set off any debt, whether or not arising out of the improved property, against the beneficiary. The Saskatchewan legislation, on the other hand, confines the right of setoff to a claim arising out of the project. The view of the Task Force was that the Saskatchewan legislation was more compatible with the expectations of the parties on the project. While the owner should not have to pay more than he owes to the contractor, those working on the project should be able to assume that the contractor will be paid the full contract price, subject only to any claims between the owner and the contractor arising out of the project on which they are working.

7. Funds Advanced, or Borrowed and Advanced, by the Trustee:

If a trustee uses his own funds, or borrows funds, to pay a beneficiary, it would seem fair that the trustee should be able to recover those funds, or to repay any lender if the funds were borrowed, from funds received that would otherwise be trust funds. Such a provision is necessary to ensure that normal construction lending will continue. Both the Ontario and the Saskatchewan legislation permit it as well.

8. Liability for Breach of Trust:

The Task Force unanimously felt that the corporate veil needed to be pierced in order to make trust obligations meaningful. A corporation is only a legal fiction. It is individuals who make decisions.

The Task Force felt that not only should the directors and senior officers of a corporate trustee be personally liable for decisions which they make or acquiesce in which constitute breaches of trust, but also that the sanction should be relatively severe.

While Ontario relies on the Criminal Code for a breach of trust, Saskatchewan and Manitoba rely on provincial offences which catch not only the intentional, but also the negligent, breach of trust. The Task Force preferred the creation of a provincial offence for breach of trust.

The Task Force also recommends that the maximum penalty for the provincial offence should be $50,000 or three times the sum which constitutes the breach of trust, if such sum can be proven, whichever is greater, and imprisonment for a term of not more than two years less a day.

Chapter 3: The Stop Notice

I. Introduction

It is the view of the Task Force that the present lien remedy, which allows a court to order that the estate or interest of the owner in land against which a lien is registered may be sold, is both unsatisfactory and inadequate, and that a new remedy more consistent with the objective of a scheme to provide greater assurance of payment should be legislated, not as an alternative to the lien, but in addition to it. This new remedy, to be called a "Stop Notice", will focus on the trust funds rather than the land.

The lien is unsatisfactory because, as long as the owner is willing and able to pay the contractor, it seems unnecessary to encumber the owner's title in order to deal with either a single lien registered because of a contractual dispute between a subcontractor and a sub-subcontractor, or the insolvency of a subcontractor. From an owner's point of view, a lien causes serious inconvenience because registration completely brings to a halt any further advances of mortgage funds.

The introduction of trust obligations on the owner and on contractors and subcontractors substantially changes the nature of the legislation. Its effect is to shift the emphasis from a real property security system to a payment assurance scheme. While the lien remedy is adequate to enforce the former, it is, in the view of the Task Force, inadequate to enforce the latter.

The current Builders' Lien Act does not put any obligation on the owner to pay the contractor. This is true not only with respect to the contract money, but also with respect to the so-called holdback. The registration of a builders' lien presents the owner with a choice. Either he may pay certain legislatively prescribed money into court in order to have the lien discharged, or he may elect not to pay any money and run the risk of losing the land against which the lien is registered. This is a choice which is of little consolation for those subcontractors and suppliers who have either worked on, or supplied materials to, the project because, most often after foreclosure, there will be nothing left to satisfy their claims.

However, with the introduction of the trust regime proposed in this report, the owner is faced with a new set of choices in addition to those relating to the lien. Either he must pay the trust money, to the extent that any exists, or he may choose to run the risk of the severe legal sanctions, including fines and possible imprisonment, which may accompany a breach of trust. Further, a breach of trust by a corporation can also lead to personal liability of its officers and directors in addition to penal sanctions. Clearly, this is a significant change from the choices facing an owner under present lien legislation.

II. The Concept of the "Stop Notice"

Conceptually, the lien encumbers the estate or interest of the owner in the land. In the event that an owner is either unable or unwilling to pay his contractor, the registration of a lien allows lien claimants to sell the land.

The Stop Notice is totally unrelated to the land. It is a new remedy which can be used to pursue trust money. It is a separate and independent remedy, proposed in addition, and not necessarily as an alternative, to the lien.

The framework of the proposed Stop Notice can be summarized in the following manner:

1. The Stop Notice will be a document prescribed by regulation;

2. The Stop Notice will be effected by service on the owner and not by registration against the owner's land title;

3. An unpaid beneficiary, other than a contractor, may serve a Stop Notice on the owner. This will create a new trust relationship between the owner and the person serving the Stop Notice. A contractor need not serve a Stop Notice since trust obligations already exist between him and the owner;

4. The unpaid beneficiary will have 90 days from completion of his contract to serve the Stop Notice;

5. Where the owner is served with a Stop Notice by a subcontractor or supplier, he will become a trustee for the person serving the Stop Notice to the extent of the amount claimed in it. The obligation of the owner, when served with a Stop Notice, will be to set aside the amount claimed in it to the extent that trust funds are in his hands, or when trust funds come into his hands in the future;

6. The owner must, within 10 days of being served with a Stop Notice, serve an Answer, in prescribed form, on the unpaid beneficiary advising that

   (a) trust money has been set aside;

   (b) although trust money has not been set aside, it will be set aside from a source which constitutes trust money; or

   (c) no money has been set aside, nor will be set aside, and the reason for not doing so;

7. If the unpaid beneficiary who served the Stop Notice wishes the money to be paid into court, he must commence an action against his immediate trustee. The owner will be served with a copy of the Statement of Claim and will then have to pay the money previously set aside into court to the credit of the action;

8. If the unpaid beneficiary who served the Stop Notice does not commence an action against his trustee and serve the owner with the Statement of Claim within 120 days of serving the Stop Notice on the owner, the Stop Notice lapses and the owner may pay the amount set aside to the contractor without jeopardy;

9. Where an owner is served with a Stop Notice, or has trust obligations to the contractor, and is insolvent, the person who served the Stop Notice, or the contractor, as the case may be, may appoint a receiver to collect the revenue generated by the improvement or other money which constitutes trust money;

10. The service of a Stop Notice, unlike the registration of a lien, will not affect mortgage priorities and should therefore not interrupt the flow of mortgage financing.

Although the Stop Notice procedure may ultimately involve the judicial process, there is ample opportunity to resolve the problem prior to the expensive court process being invoked. It is anticipated that the 10 day period after the owner is served with a Stop Notice will create a situation in which attempts will be made to settle the matter. If the money has been set aside, it is likely that the unpaid beneficiary will not commence a legal action if there is a reasonable likelihood that the matter can be resolved. Until an action is commenced, the Stop Notice procedure is outside the legal process, unlike the registration of a lien, which immediately sets the legal machinery into operation.

III. Trust Obligations of the Owner

Previously in this report the Task Force recommended that the following funds of the owner be trust funds:

1. Funds secured by a mortgage or other security and advanced to the owner for the purpose of financing the improvement;

2. Any funds in the hands of the owner, or received by the owner, for payment of the improvement;

3. Any funds, or source of funds, identified by the owner to the contractor as being funds earmarked for paying the costs of the improvement;

4. Any funds derived from a bona fide sale of the improvement by the owner, subject to prior encumbrances and normal expenses;

5. The net proceeds from insurance should the improvement be damaged or destroyed; and

6. Any revenue generated from the improved land, subject to prior encumbrances.

It should be noted that, in the context of the oil and gas industry, "land" includes all wells which are included in the particular licence or lease.

The imposition of trust obligations creates by implication a duty to pay. Trust money must be paid by the owner to a beneficiary regardless of any remedy that may exist with respect to the land. That is, the owner will no longer have the option, as he does now, of electing to let the land go if there are trust funds in existence. The importance of determining at the time of contracting exactly which funds are "trust" funds should be obvious and it is expected that such will be defined in contracts in the future.

If trust funds are not paid, penal sanctions may be imposed on the owner, and, if the owner is a corporation, possibly on its officers and directors. As well, if there is a breach of trust by a corporation, its officers and directors may be personally liable for damages resulting from the breach.

It must be emphasized that, in the absence of the Stop Notice, an owner would have a trust duty only to the contractor. Thus, under the Ontario and the Saskatchewan legislation, which have no Stop Notice provisions, subcontractors and suppliers have only a lien remedy against the owner. In those provinces, subcontractors and suppliers have no remedy to pursue trust funds in the hands of the owner. However, with the Stop Notice, unpaid beneficiaries may pursue both trust funds and the land.

The Task Force recommends that both subcontractors and suppliers should be permitted to serve a Stop Notice on the owner. Once this Stop Notice is served, the owner's trust obligations will extend beyond the contractor to those persons who have served Stop Notices. The owner can then only discharge his trust obligations to those persons who have served the Stop Notices by setting aside the amount claimed.

It is possible to enforce the trust claim and the lien claim either simultaneously or separately. Any shortfall in a lien claim could be supplemented by a trust claim and any shortfall in a trust claim could be supplemented by a lien claim.

It may be helpful to consider the following examples:

1. Consider the case of an operator of an oil well who is also a joint venture participant. Elsewhere in this report, the Task Force recommends that a person who earns an interest in land as a result of doing, or causing to be done, any work on, or in respect of, an improvement should have the same trust obligations with respect to the same funds as an owner. Once the operator receives money from the other joint venture participants for the purpose of funding the cost of drilling the well, that money becomes trust money in his hands for the benefit of the contractor. Once work is performed, the contractor would have a lien claim and a trust claim under this proposal. Subcontractors and suppliers would continue to have a lien claim and would have a trust claim on the operator if they serve a Stop Notice on him.

2. Assume that an oil well has been successfully drilled and put into production and that the contractor and some subcontractors have not been paid. It has been previously recommended that revenue from the land improved should constitute trust funds in the hands of the owner. In the absence of a Stop Notice from subcontractors, the owner would have a trust obligation only to the contractor. However, the subcontractors could serve a Stop Notice on the owner and appoint a receiver to collect the revenue from the sale of the oil.

3. Suppose a builder has arranged bank mortgage financing and anticipates that his equity in the improvement will come from the sale of another project. Further, assume that the project is virtually complete but the funds of the owner have not yet materialized because the other project which was to be sold was not sold. Finally, assume that land values have declined and that the owner has decided to abandon the improvement.

It should be recalled that the Task Force has recommended that funds, or a source of funds, identified by the owner to the contractor as funds to be used for the financing of the improvement should constitute trust funds. If the contractor had requested an identification of the funds, or the source of the funds, for payment of the improvement, and the proceeds of sale of the other project in our example had been identified as such, then they would be trust funds once the other project had been sold. Not only the contractor, but also subcontractors and material suppliers, if they had served a Stop Notice on the owner, could make trust claims with respect to those funds as well as enforcing their lien claims against the land improved.

It is expected that many owners will be requested to identify in their contracts the source of funds for financing the project in order to convert any funds so identified into trust funds, if they would not otherwise be trust funds.

The Task Force was of the view that the wording of section 6(2) of the Saskatchewan legislation which states that "the moneys in the hands of the owner or received by him for payment under the contract at any time thereafter constitute a trust fund for the benefit of the contractor" was vague and could lead to considerable difficulty in a court's identifying trust funds. It appears to the Task Force that a prudent contractor and a responsible owner would have little difficulty in identifying funds, or a source of funds, available for financing an improvement.

4. Assume that the owner is solvent but that a subcontractor is not. The beneficiaries of the insolvent subcontractor can serve a Stop Notice on the owner. Any trust funds remaining in the hands of the owner up to the amount claimed in the Stop Notice would have to be set aside by the owner or else he would be in breach of trust.

IV. Conclusion

The concept of a Stop Notice is not entirely new. Although it is not used in any Canadian jurisdiction, it is an integral part of the lien system in California.

The Task Force is of the view that, since it does not encumber the land, the Stop Notice will not engender the strong adverse reaction that the registration of a lien does now. The Task Force heard a significant number of representations from smaller contractors who indicated strong reluctance to register a lien since to do so often makes it difficult to find future work, especially during difficult economic times. Since the service of a Stop Notice does not affect priorities, it is unlikely that a Stop Notice will stop the flow of funds as does the registration of a lien.

With the adoption of the Stop Notice, in those circumstances where the solvency of the owner is not an issue, the Task Force anticipates that, over the course of time, less reliance will be placed on the lien and greater reliance on the Stop Notice. The lien will be looked to only if the intention is to sell the land of the owner. In reality, most subcontractors and suppliers have little interest in the land of the owner because there is little likelihood of their achieving satisfaction from its sale.

The Stop Notice is a much more versatile remedy than is the lien. It survives mortgage foreclosure and attaches to any unexpended trust funds. It is a means by which subcontractors and suppliers may effectively pursue trust funds without incurring the stigma associated with the registration of a lien. This is beneficial not only to the subcontractors and suppliers but also to owners. In the final analysis, the Stop Notice is the logical mechanism to enforce the trust regime being proposed in this report.

Chapter 4: Elimination of the Statutory Holdback

I. Introduction

The initial concept of builders' liens was to grant security to the builder for the improvement resulting from his efforts, based on the proposition that the owner should not be unjustly enriched by the efforts of others. Accordingly, if an owner did not pay, the contractor could claim a statutory lien on the owner's property, as well as being able to pursue his contractual remedies. The concept has logical appeal and all jurisdictions in North America have lien legislation of one sort or another.

II. The Holdback

The "holdback", as it is referred to, is the statutory obligation of the owner to retain 15 percent of the value of the work actually done and materials actually furnished when making a payment on the contract. It was introduced in Alberta in 1930: S.A. 1930, c. 7, s. 14(1)(2). The holdback is a concept related neither to lien rights per se nor to the principle of unjust enrichment. Most American jurisdictions with lien legislation, for example, do not have a statutory holdback requirement. The initial concept of the holdback appeared to be that the profit of the contractor should be retained by the owner as security for the subcontractors and material suppliers.

In reality, the holdback in Alberta is not a specific pool of money retained by the owner, but is rather a notional concept which only comes into being in the event that the owner decides to pay it into court in order to clear his title of liens. As Mr. Justice Crossley put it in **Northern Eau Claire Construction Materials** v. **Pruett et al**, 83 A.R. 155, 57 Alta. L.R. (2d) 140 (Alta.Q.B.):

> "The [Builders' Lien Act] does not create a trust fund for lien claimants. The lien fund is simply a notional concept. The Act only provides one situation where the lien fund becomes accessible for lien claimants. This occurs where the owner pays money into court under s. 18 or s. 35(1). If the owner does not do this, the lien claimant cannot compel payment into court nor can he gain access to the lien fund.
>
> If the owner does not retain the lien fund, the estate or interest to which the lien attaches under s. 4 remains liable for the lien. In such a case, a lien claimant (who does not have privity of contract with the owner) can realize on the lien through a sale of the estate or interest to which the lien attaches pursuant to s. 45(2)." (A.R. at page 159, Alta.L.R. (2d) at page 145)

III. The Rate of Holdback

If the protection of lien claimants were paramount, logic would dictate that the percentage of funds retained as a holdback should be increased, yet exactly the opposite has occurred. As the British Columbia Report put it in considering the possibility of increasing the holdback percentage,

> "... the best approach to this problem is to recognize quite frankly that however one tries to tinker with the holdback, the more money that is required to be held back, the more the flow of funds is likely to be inhibited. Ultimately, a choice must be made between building in protection for the lien claimants at the expense of slowing down the flow of funds, or assisting the flow of funds at the expense of a measure of protection to the lien claimants." (at page 39)

The British Columbia Report concluded that,

> "In the light of the logic of representations from members of the construction industry that concentration should be placed on improving the flow of funds...", (at pages 39-40)

the holdback should be maintained as 15 percent rather than being increased to 20 percent.

The Manitoba Report concluded that

> "As a further and final attempt by us to increase the flow of funds to the industry without thereby significantly reducing the existing protections to builders, we also recommend a reduction in the holdback from 15% and 20% to a fixed amount of 7½%. The Commission believes that such a reduction will likely speed up the flow of funds and in addition will provide some test as to whether or not a holdback of any amount is required." (at pages 56-7)

The Ontario Report stated that the proposed reduction of the rate of holdback from 15 percent to 10 percent "was one of the most controversial proposals":

> "... any reduction in the holdback will result in a reduction in the security afforded to construction suppliers by the holdback provisions of the Act. The holdback is often the only amount available to satisfy lien claims. Reduction in the rate of holdback will often mean that there will be less money available to satisfy these claims... However, the Committee as a whole has come to the conclusion that the rate of holdback should be reduced to 10 percent. In the opinion of a majority of the Committee, the present rate of 15 percent is unrealistically high, and has amounted to a severe hardship to contractors and subcontractors. A contractor or subcontractor must normally pay his workers and material suppliers in full. The present rate of holdback often requires contractors and subcontractors to borrow extensively to obtain the necessary operating funds to enable them to pay for their materials and labour. Such borrowing can only be reflected in the costs of construction, and may result in an increase in the risks of an insolvency on the project. The possible insolvency of a contractor or principal subcontractor imperils the completion of the project, and the real security of everyone involved in its construction." (at pages xxx-xxxi)

Commenting on the reduction of the holdback to 7½ percent in Manitoba, the Ontario Report stated that

> "Reduction of the holdback to this level would substantially erode the protection it affords to subcontractors, workers and material suppliers of an insolvent contractor or subcontractor. Where the contractor defaults in the performance of the contract, the holdback may be the only money available to satisfy the lien claimants. Every reduction in the holdback, including the reduction of 15 to 10% recommended by this Committee makes it less worthwhile to pursue a lien claim, since the amount available to satisfy the claim is also reduced. However, reduction of the holdback below 10% in the opinion of the Committee, would reduce the protection afforded by the Act below an acceptable level." (at page xxxii)

The Saskatchewan Report recommended a reduction in Saskatchewan's holdback rate from the 15 percent and 20 percent rates then applicable to 10 percent, feeling "that it would be difficult to resist the trend to a lower rate...". (at page 121)

Thus, at the present time, the holdback is 10 percent in Ontario, Saskatchewan and British Columbia and 7½ percent in Manitoba. It is interesting to note that most American jurisdictions do not have any statutory holdback.

IV. Securing the Holdback

Besides the rate of the holdback, another issue which has occupied much of the law reform effort has been the problematic nature of its existence. While the legislation has required the owner to hold back a certain percentage of the contract price, it has never forced that "notional" holdback to be any more than exactly that. In other words, the owner has never been forced to isolate the holdback into a separate pool of money. As Professor Darby put it in his Study Paper prepared for the Nova Scotia Report, while the holdback is "thought of as an existing sum of money to which the lienholder has ready access to secure his claim against default in payment by the person primarily liable to him", in fact, the holdback is

> "merely a device by which a party may limit his liability in a mechanic's lien action to the amount directed to be retained by him in favour of the lien claimants. It permits an owner to finance a project to the extent of eighty-five percent of the contract price, until the date on which the holdback is paid out to those entitled to it. In fact, the holdback is not usually an existing sum of money at all." (at pages 96-7)

The Manitoba Report saw the "need for creating an actual, as opposed to a notional, holdback fund that will be available for payment to the appropriately entitled persons." (at page 50) It recommended a system under which the holdback would be paid into an interest-bearing account in the joint names of the owner and the contractor. The Report viewed this proposal "as the best means of obtaining the objectives of a holdback fund." (at pages 55-6) Section 24(3) of Manitoba's legislation provides that where the contract price exceeds $200,000.00, "... the owner shall, as the work is done, the services provided and the materials supplied under the contract, pay the holdback into a holdback account."

The Ontario Report rejected the Manitoba scheme as "the costs of the joint trust account proposal would far exceed its benefits." (at page xxxv) However, the Report was of the view that there was a need to secure the holdback:

> "We agree that there have been numerous occasions on which lien claimants have found the owner's interest in the premises to be insufficient to satisfy claims in respect to the holdback. In the experience of the Committee, this situation normally arises as a result of erosion of the owner's equity in the premises as a result of the accumulation of arrears in interest, where the owner defaults in the payment of a mortgage. Since the relative priority between mortgages and the liens are the cause of the problem, we believe that the best way to resolve the problem is to adjust those relative priorities so as to protect the lien claimant's rights in the premises. To do this, we propose to give lien claimants priority to the extent of any deficiency in the holdback over every mortgagee who takes a mortgage for the purpose of securing the financing of the improvement ('building mortgage'), and also over any mortgagee who acquires an interest in the premises subsequent to the commencement of the making of the improvement, irrespective of the purpose of that mortgage." (at pages xxxvi-xxxvii)

The Saskatchewan Report agreed that the holdback must be secured as it "represents money already earned by those who have provided materials or services to an improvement and, in this regard, should be secured for the benefit of those persons who have earned it." (at page 128) The Report considered but rejected the Ontario approach of securing the holdback by giving liens a stronger priority over prior mortgages. The Report was concerned that this would

> "appear to adversely affect the possibility of obtaining credit on construction projects. It would require a greater intervention by the financial community into the paying out of the holdback and could possibly slow down its release. The mortgage priority would be a solution that would require the parties to litigate. In the event of default before completion, the issues as to the amount of the holdback, determining the work done to date and determining the amount of the claims would have to be resolved through the litigation process. There would be no records as there would be with the holdback trust account concept to assist the parties in determining crucial dates and amounts." (at page 130)

The Saskatchewan Report rather was attracted to the concept of a joint trust account for a number of reasons:

> "Clearly, lien claimants, with knowledge of the existence of a joint trust account for the holdback, would be and feel more confident that the holdback will be paid to them. Furthermore, requiring the owner to place the holdback into a joint trust account would be a means of determining the amount of the holdback and determining the work done to date and, to some extent, determining the amount of the claims if default occurs before completion of the project. All of this would be in addition to the primary purpose for the creation of the joint trust account and that is to secure the holdback in the event of default or abandonment of the contract." (at pages 129-30)

V. Elimination of the Holdback

Elimination of the statutory holdback has not been recommended in any of the reports canvassed. The OLRC Report rejected a call by the Board of Trade of Metropolitan Toronto to eliminate the holdback. The Board of Trade's proposal read as follows:

> "It is proposed that all sections of the present Act, which require a holdback from payments to contractors or which refer to the release of such holdback, be completely eliminated. Nothing in the revised Act will require or authorize a holdback with the result that any holdback arrangements between contracting parties must be mutually agreed to in their contract...
>
> It is recognized that, if the Lien Act does not require a holdback, many owners and general contractors will provide for a holdback as a term of most contracts they let. These holdbacks in many cases may be expressed as a percentage of the contract price but it is reasonable to expect that they should not be nearly as large as the present 15% statutory holdback and the terms of their release should be much less strict than is presently the case." (at page 6)

This proposal was rejected in the OLRC Report:

> "... we are opposed to the abolition of the holdback provisions. To rely on voluntary holdbacks would, in our view, be detrimental to the interests of those for whose benefit the Act has been passed." (at page 11)

The holdback is not a fund in most cases. The owner often defers borrowing the 15 percent holdback until after the lien period has expired, even though the owner could pay the holdback after substantial completion. Furthermore, it is the practice that no holdback is retained from material suppliers. It is the contractor and the subcontractors therefore who must finance the difference between the receipt of funds and their labour, material and overhead costs. This deficiency in cash flow is a serious problem and itself often leads to insolvencies and business failures, especially for those in the construction industry who have a low ratio of equity to receivables in their business.

The owner is not personally liable for the 15 percent holdback. If the owner is the one who defaults in payment, the only recourse is the registration of a lien against his property. In most cases, a lender will have a mortgage that ranks ahead of the liens. As well, interest accumulated on the mortgage arrears has priority over the liens. Thus, it is a rare circumstance when a lienholder has security, because of the holdback provisions, in the event of the owner's default, since the lender's priority generally leaves nothing for lienholders and since there is no actual pool of money in existence.

Manitoba, Saskatchewan and Ontario each addressed the issue of securing the holdback and resolved it by different means. Ontario gives the lien priority over any other security to the extent of any deficiency in the 10 percent holdback while Manitoba and Saskatchewan require that the holdback be placed in a separate joint trust account.

The Task Force heard that the contractor on most large projects in Alberta is required to provide Material and Labour Payment Bonds, and, often, Performance Bonds. For these projects, reliance is generally not on the statutory holdback requirement or the Builders' Lien Act. For example, the Public Works Act does not require a holdback. Nevertheless, the government requires bonding and, depending on the size of the project, contractually provides for the retention of a holdback.

On mid-size projects, the custom varies. Bonds may or may not be required. However, when one deals with residential construction or the small commercial building sector, there is virtually no bonding and greater reliance on the Act is the rule.

In a practical sense, the lien is the primary security for the contractor, while the holdback is the primary security for the subcontractor.

The issue which the Task Force debated was whether or not the statutory holdback provides any "real" security. The word "real" is emphasized since, at first glance, one would assume that it does. However, representations to the Task Force on this issue were as follows:

1. If there is any reasonable hope of payment, a lien is not registered because the registration of a lien creates such antagonism that the lien claimant, if a subcontractor, faces a high risk of developing a reputation that is detrimental to continued acceptance in the industry, especially if the construction sector has over-capacity. Yet, it is during times of economic recession that most defaults occur;

2. In case of a default by the owner, the lien claimants are, in most cases, foreclosed by the lender;

3. In cases of the contractor's default, the owner often incurs substantial additional expenses in completing the project. The lien fund will be relatively small in relation to the total claims and, when combined with the costs of litigation, will often leave little for the lien claimants; and

4. The lien system does work for the isolated lien. In such a case, the problem is most often between the contractor and a subcontractor or between the subcontractor and a sub-subcontractor. In such a situation, the lien is registered and the dispute is generally resolved without reliance on the holdback, although the owner does apply pressure to resolve the problem.

The Task Force was briefed on the California Lien Law where no statutory holdback is required. In California, owners generally retain a contractual holdback between seven and 15 percent, depending on the size of the project. The average holdback in California is about 10 percent, but would be reduced if adequate bonding were in place.

The Task Force is not proposing that Alberta adopt the California system, but recommends that the statutory holdback be eliminated. This will result in an increased flow of funding which, when combined with the comprehensive trust and Stop Notice provisions previously recommended, will, in the view of the Task Force, provide superior security and greater assurance of payment for subcontractors and suppliers.

VI. Simplification of the Legislation

An important factor in the decision of the Task Force to recommend elimination of the statutory holdback is the resulting statutory simplicity. The present legislation is universally thought to be terribly complex and virtually unintelligible.

Section 15(1) imposes an obligation on an "owner" to withhold 15 percent of the value of the work actually done and materials actually furnished for a period of 45 days from the date of completion of the contract or from the date of issue of a certificate of substantial performance. Subsection (2) of section 15 imposes a further obligation on the owner while a lien is registered against his land title, namely, to withhold, in addition to the 15 percent, "any amount payable under the contract that has not been paid under the contract that is over and above the 15%."

Where a certificate of substantial performance is issued pursuant to section 15.1 of the Act, a further holdback obligation arises under section 16.2(1), namely, to retain 15 percent of the value of the work actually done and materials actually furnished from the date of issue of the certificate of substantial performance until 45 days from the date of the completion of the contract.

"Substantial performance" is a triggering mechanism for allowing the owner to release the holdback before the completion of the contract to which it relates. It is a term of art and is dealt with in section 2 of the Act which basically provides that a contract or a subcontract is substantially performed when the improvement is ready for use and 97 percent of the work has been completed.

With the elimination of the holdback, the above would become irrelevant in the sense that, with no statutory obligation on the owner to withhold 15 percent of every contract payment, there need be no statutory formula with respect to when the holdback may be released. Thus, sections 15, 15.1, 15.2, 16, 16.1, 16.2, 16.3 and 16.4 of the Act would become generally inapplicable.

In section 1 of the Act, the "definition" section, the following definitions would not be required:

(a) "certificate of substantial performance",

(f.1)"lien fund",

(f.2)"major lien fund", and

(f.3)"minor lien fund".

Section 2, the statutory description of when a contract or subcontract is substantially performed, would also become irrelevant as would section 2.1.

The elimination of the indicated sections of the Act will remove much of the statutory complexity which at the present time plagues most persons attempting to make sense of it. If there is to be a holdback, it will be a contractual matter, the result of usual contractual negotiation.

VII. Conclusion

The Task Force felt that there is a serious misunderstanding in the construction industry, especially in the residential and small commercial building sectors, about the degree of security that the Builders' Lien Act provides. This reliance leads to poor business practices. Proper credit checks and formal contractual relationships are often overlooked because contractors and subcontractors believe that the Builders' Lien Act constitutes adequate protection for them. Elimination of the statutory holdback, in the view of the Task Force, should encourage better business practices.

With the elimination of the statutory holdback, it is expected that owners will contractually insist on a holdback. It is highly likely, therefore, that funds will remain in the owner's hands, even after most subcontractors complete their work. Such funds would be caught by a validly registered lien, or a properly served Stop Notice. However, once the owner, in good faith, has paid the contractor the full amount owing, the lien or the Stop Notice will attach to nothing.

Ideally, the construction and oil and gas industries should function as smoothly as possible and as unencumbered as possible. Contracts should determine rights and good business practices should determine who receives credit. Elimination of the statutory holdback, with the addition of comprehensive trust provisions, should move the industries in that direction.

Lastly, the question of whether or not the statutory holdback should be eliminated was posed to all those who appeared before the Task Force. None objected and many strongly endorsed the concept, including the Alberta Construction Association.

With the imposition of the statutory trust and its complementary remedy, the "Stop Notice", the Task Force is of the view that the trade-off between the relatively modest security provided by a 10 percent holdback and the increased flow of funds and simplification of the Act as a result of its elimination, favours elimination of the statutory holdback.

Chapter 5: Oil and Gas

I. Introduction

The economic downturn experienced in the construction industry in the early 1980s was felt in the oil and gas sector as well. During these years, as insolvencies became more frequent, subcontractors and suppliers in the industry began to pay more attention to the Builders' Lien Act as a collection vehicle. As such, the legislation was perceived by the industry to have several deficiencies which were made known initially to the government and subsequently to the Task Force.

While the construction industry and the oil and gas industry share many common factors, some differences exist which may require differential treatment under the Builders' Lien Act.

II. Legislative History

In Wakefield Co. v. Oil City Petroleums Ltd. [1958] S.C.R. 361, an Alberta case, Mr. Justice Rand stated that the

> "early exploitation of oil and gas resources in the Province raised questions of difficulty under the earlier provisions of the Act and special terms were enacted by the Legislature by 1943, c. 31, s. 12, in ss. 43 to 47..." (at page 365)

Those provisions read as follows:

> "43. The definition of 'owner' as set out in paragraph (g) of section 2 shall include, in addition to the persons therein set out, every person having any estate, interest or right in the oil or gas in place or in the oil or gas when severed, notwithstanding that such person has not requested the contract work to be done, is only indirectly benefited thereby and has had no dealing or contractual relationship with the contractor or person claiming the lien:
>
> "Provided, nevertheless, that where the oil or gas is held in fee simple, the holder of an interest in the first royalty in the oil or gas, up to twenty per cent thereof, shall not, by reason of this section, be deemed to be an owner.
>
> "44. The lien provided by section 6 shall not only attach to the land, including the oil and gas therein, but also to the oil and gas when severed.
>
> "45. All interests in the oil or gas under any lease, mortgage or agreement for sale relating to the oil or gas in excess of the said first royalty up to twenty per cent shall be subject to the lien in all respects and the provisions of sections 10 and 11 shall not be applicable thereto.
>
> "46. It shall not be necessary to set out in the claim for lien set out in section 19 the name of the owner or alleged owner and the provisions in that regard contained in the forms in the Schedule shall not be applicable in the case of oil and gas wells.
>
> "47. In appointing a receiver pursuant to section 36, the judge may, in addition to the powers therein conferred on such receiver, authorize him to take charge of the well and operate it and sell the production therefrom or, in the alternative to take the oil and gas when produced and saved and sell the same and receive and pay into court the proceeds of the oil and gas when sold."

Section 43 [S.A. 1943, c. 31, s. 12] expanded the definition of "owner" and, according to Mr. Justice Rand in the above-noted Wakefield case,

> "was undoubtedly passed to meet ... conditions brought about by the urgency to exploit the resource in which formal agreements could not keep pace with action and only by relation back were the rights of the parties intended to be determined." (at pages 369-70)

Section 44 extended the lien to the oil and gas when severed. Section 46 removed the necessity to set out in the claim for registration the name of the owner. Section 47 added to the powers which could be conferred on a receiver, appointed under the legislation, to authorize him either to operate the well or to take the oil and gas when produced, sell it and pay the proceeds into court. As Rand J. explained, "These sections, because of the special character of the subject-matter, create additional and cumulative liens." (at page 366)

Further provisions were added in 1952 dealing with liens on minerals held from the Crown as S.A. 1952, c. 51 s.6:

> "48. (1) Where a lien is claimed in respect of property which consists of, —
>
> "(a) any mine; or
>
> "(b) any well drilled for the purpose of obtaining oil, gas or other mineral; or
>
> "(c) any work or operation conducted preparatory thereto;
>
> and if the property is held under any claim, lease, license, permit, reservation or other agreement from the Crown granted pursuant to the *Dominion Lands Act*, or pursuant to *The Provincial Lands Act*, or pursuant to *The Mines and Minerals Act*, or by some person claiming by, through or under any holder of such claim, lease, license, permit, reservation or other agreement, the claim for registration of the lien shall be made to the Minister of Mines and Minerals instead of to the Registrar of Land Titles.
>
> "(2) No lien may be filed pursuant to the provisions of subsection (1) in respect of a claim for wages for the payment of which security has been lodged pursuant to *The Industrial Wages Security Act*.
>
> "(3) The provisions of this Act as to registration by the Registrar of Land Titles shall apply, *mutatis mutandis*, to registration hereunder by the Minister, and upon registration, the lien shall be enforceable as against the interest of the holder of the claim, lease, license, permit, reservation or other agreement as aforesaid in the same manner as a lien duly registered pursuant to section 19.".

These provisions were consolidated in the 1955 revision as: R.S.A. 1955, c. 197, ss. 49-56. Section 28 of that legislation set the time for registration of a lien in the case of oil or gas wells, or oil or gas pipelines as 120 days after the completion of the improvement. The Buchanan Report recommended that there should be a uniform 35 day period for registering liens throughout the legislation and this recommendation was carried out in the 1970 Builders' Lien Act.

III. Discussion of the Task Force's Recommendations

It is generally agreed that most of the content of the existing Builders' Lien Act applies to the oil and gas industry.

The Task Force consistently heard that there is no partial release of the holdback upon substantial completion of the contract in the oil and gas industry. If this is the case, the elimination of the statutory holdback should not cause any disturbance in the industry.

As well, the proposed registration of contractors and subcontractors should logically apply as well to those who operate in the oil and gas industry. Even more so, some might argue, because of the inherent risk in the oil and gas industry where heavy initial costs, for example, for exploration and drilling, are required before any trust funds will be available for distribution.

Because many owners enter into farmout arrangements in which a farmee will earn an interest in the land upon drilling being completed successfully, and therefore no money flows between the owner and the farmee, the Task Force recommends that the funds of the farmee used for the improvement be trust funds to the same extent as if he were an owner. That is, a person who earns an interest in land as a result of doing, or causing to be done, any work on, or in respect of, an improvement should have the same trust obligations as an owner has with respect to:

(i) money borrowed and advanced by the lender for the purpose of financing the improvement;

(ii) any funds in the hands of the owner, or received by the owner, for payment of the improvement;

(iii) income derived from the lands improved;

(iv) funds, or a source of funds, identified by him for the purpose of financing the improvement;

(v) net proceeds of sale of the improved lands; and

(vi) net insurance proceeds from the improvement.

It should be noted that in this context "land" includes all wells which are included in the particular licence or lease.

It is also generally agreed that the trust provisions which the Task Force is recommending should apply to both the construction and the energy sectors. The owner's trust for the proceeds of sale of oil and gas should be especially helpful in overcoming some of the difficulties peculiar to the oil and gas industry. Unlike the construction industry, the end product in the energy sector may be either a wasting asset or worse, a dry well. If the owner's interest is a licence or a lease which includes producing wells, the owner's trust will include the revenue generated by those other wells, provided that the interest is held by the same owner.

The ability of a lien to "attach" oil and gas revenue has recently been the subject of judicial comment both in Saskatchewan and in Alberta. In **Canada Trust Company v. Cenex Limited**, [1982] 2 W.W.R. 361, 131 D.L.R. (3d) 479, 13 Sask.R. 435, Mr. Justice Hall of the Saskatchewan Court of Appeal held that, in a contest between lienholders and debenture holders, the claims of the lienholders had priority over those of the debenture holders with respect to severed ore. At the time the case was decided, section 12(3) of the Saskatchewan Mechanics' Lien Act provided that:

> "A lien attaching to an estate or interest in mines and minerals attaches also to the minerals when severed and recovered from the land while they are in the hands of the owner, and to the proceeds thereof and to the amounts to be paid in lieu thereof to the owner by a person that operates the mine, oil well or gas well in accordance with an order or regulation made under The Mineral Resources Act."

Mr. Justice Hall justified this result in the following manner:

> "This legislation does not, in the ordinary way, deprive the debenture-holders of pre-existing rights. Before the ore was extracted, their security covered the mine and minerals in situ. The work and materials supplied by the lienholders have transformed the mineral in situ into readily marketable ore and have greatly enhanced its value. The legislature has recognized that this entitles the lienholders to first claim upon the severed ore." (W.W.R. at page 365)

It should be noted that a receiver had already been appointed by the court in that case to take over the assets when Cenex Limited defaulted under the terms of the debentures.

The result in the above-noted **Cenex** case was seriously questioned in the Saskatchewan Report:

> "Turning subsection 12(2) into a section establishing a priority rule creates serious consequences for financers of mining and oil and gas interests." (at page 112)

The Saskatchewan Report concluded that

> "there was a justification for extending the lien on land and materials to severed minerals and to the equipment of the owner. When there is default in the oil and gas industry, there is little for the lien claimants to attach in the way of an improvement and resort must be had to the personal property of the owner. However, this lien should only be an extension and not a different lien from the lien currently created by subsection 12(1) as found by the **Cenex** case. The priority rules for all liens would then continue to apply. The only priority a lien claimant would have in relation to severed minerals or equipment would be priority over unsecured creditors." (at page 113)

The Saskatchewan Report therefore recommended that:

1. The lien on the land and materials should also extend to severed minerals, etc., and equipment, etc., owned by the owner recovering the minerals; and

2. The general priority rules would then apply to the lien as extended. (at page 114)

Section 22(2) of the Saskatchewan Builders' Lien Act which followed the Saskatchewan Report provides that:

> (2) Where services or materials are provided:
> (a) preparatory to:
> (b) in connection with; or
> (c) for an abandonment operation in connection with;
> the recovery of a mineral, then, notwithstanding that a person holding a particular estate or interest in the mineral concerned has not requested the services or materials, the lien given by subsection (1) is also a lien on:
> (d) all the estates or interests in the mineral concerned, other than the estate in fee simple in the mines and minerals, unless the person holding that fee simple has expressly requested the services or materials;
> (e) the mineral when severed and recovered from the land while it is in the hands of the owner, and to the proceeds of the mineral and to the amounts to be paid in lieu of the proceeds of the mineral to the owner by a person that operates the mine, oil well or gas well;
> (f) the interest of the owner in the fixtures, machinery, tools, appliances and other property in or on the mines, mining claim or land, oil or gas well and the appurtenances thereto;
> but, in all other respects, this Act applies to the lien existing by virtue of this subsection notwithstanding that the lien extended by clauses (e) and (f) is a lien on an interest in personal property.

Presumably, section 22(2) adopts the recommendations of the Saskatchewan Report and in the result reverses the Cenex decision.

In Alberta, section 4(3) of the Builders' Lien Act is slightly different in wording, although probably not in effect, than Saskatchewan's section 12(3). Section 4(3) provides that "A lien attaching to an estate or interest in mines and minerals also attaches to the minerals when severed from the land." Thus, Alberta's legislation does not expressly extend the lien to the proceeds of sale of the severed minerals.

However, in **Alberta Gold Well Servicing Corp. v. Snow Hawk Energy Inc.**, 53 Alta. L.R. (2d) 333 (Alta.Q.B.), Master Funduk found that "the lien extends to the net sale proceeds held by the trustee". (at page 335) In **Halliburton Services Ltd. v. Snowhawk Energy Inc.**, 57 Alta. L.R. (2d) 258 (Alta.Q.B.), Halliburton, which had valid builders' liens, filed a proof of claim with Snowhawk's trustee in bankruptcy claiming payment of funds initially attached by way of garnishee summons. Because the sale took place prior to the assignment into bankruptcy, and prior to the appointment of a receiver, Mr. Justice Forsyth held that, in the circumstances,

> "To attach the liens to the proceeds of sale... would be an unwarranted extension of the law. To attach the proceeds of sale of oil and gas a court-appointed receiver or trustee must effect the sales." (at page 263)

The Task Force is not recommending any change with respect to the manner in which the lien operates. However, once the minerals are converted to money, it becomes subject to enforcement through the trust procedure. It appears unnecessary to the Task Force to create a lien on the proceeds as well. In fact, this appears to be inconsistent as the beneficial interest already belongs to the beneficiary.

Lastly, the oil and gas industry requested an extension of the period within which to register a lien from the present 45 days to 90 days. It should be noted that, prior to the legislation resulting from the Buchanan Report, the lien period in the oil and gas industry was 120 days. In light of the payment practices in the industry, the Task Force recommends that the period within which to register a lien in the oil and gas industry should be increased to 90 days.

Chapter 6: Appointment of a Receiver

Prior to the 1985 amendment of the Builders' Lien Act, the sections of the legislation dealing with the appointment of a receiver or trustee read as follows:

> "(1) At any time after service of the statement of claim, any party may apply to the court for the appointment of a receiver of the rents and profits from the property against which the claim of lien is registered, and the court may order the appointment of a receiver on any terms and on the giving of any security or without security as it considers appropriate.
>
> (2) At any time after service of the statement of claim, any party may apply to the court for the appointment of a trustee and the court may, on the giving of any security or without security as the court considers appropriate, appoint a trustee
>
> (a) with power to manage, sell, mortgage or lease the property subject to the supervision, direction and approbation of the court, and
>
> (b) with power on approval of the court to complete or partially complete the improvement." (R.S.A. 1980, c. B-12, s. 40)

In 1985, section 40 was amended to provided that, although a statement of claim did not have to be "served", it did have to be "issued" before an application could be made for the appointment of a receiver or a trustee. (S.A. 1985, c. 14, s. 24)

Both Ontario and Saskatchewan provide that any person having a lien or any other person having an estate or interest in the land may apply to the court for the appointment of a receiver.

As the Task Force did not receive any submissions with respect to the appointment of a receiver, it does not recommend any change to the existing provisions. However, the Task Force does recommend that an unpaid trust beneficiary should be able to apply to the court for the appointment of a receiver for any funds that would otherwise come into the hands of the trustee. Recalling the earlier recommendation that all revenue generated by an improvement should become part of the owner's trust, the appointment of a receiver to receive trust funds would be particularly attractive in the oil and gas industry where banks may not crystallize their security in the event of an otherwise reasonably solvent owner who runs into trouble on a single well. In such a case, where the encumbered land generates revenue, unpaid drilling contractors, for example, may have a source from which to satisfy their claims.

Chapter 7: Licensing or Registration

I. Introduction

The Task Force repeatedly heard that a number of contractors and subcontractors are, simply put, unscrupulous. For instance, an unscrupulous contractor may underbid a legitimate contractor with no intention of paying in any event or, at least, being unconcerned about paying subcontractors and material suppliers. When these contractors become insolvent, they leave bad debts behind and open a business under the umbrella of another corporation. Somehow, they continue to function and cause considerable disruption and losses in the industry. Obviously, such conduct disturbs the economic stability of the industry and as a result is not beneficial to it.

The trust provisions and the consolidated trust account which are being recommended in this report can only be effective if contractors and subcontractors understand and comply with their obligations as trustees. Legislation itself cannot prevent the losses caused by unscrupulous contractors or subcontractors.

At the present time, it appears that no other province licenses or registers contractors or subcontractors. Neither the Ontario Report nor the Saskatchewan Report addressed the issue of licensing. In California, all contractors and subcontractors are required to be licensed.

In Alberta, there are very few instances where persons handling sizeable trust funds are not licensed. For example, both real estate agents and security traders are either licensed or registered: see, Real Estate Agents' Licensing Act, R.S.A. 1980, c. R-5, s. 3(1); Securities Act, S.A. 1981, c. S-6.1, s. 54(1)(a).

The Prepaid Contracting Business Licensing Regulation (Alberta Regulation 314/82 as amended by Alberta Regulation 127/87) passed pursuant to the Licensing of Trades and Businesses Act, R.S.A. 1980, c. L-13, already subjects home renovators to a licensing requirement:

> "3(1) No person shall carry on or engage in the prepaid contracting business unless he holds a prepaid contracting business licence issued under this regulation."

Further, an application for a licence or a renewal of a licence must be accompanied by a bond. [s. 12(1)] A licence issued pursuant to this Regulation terminates if the bond provided by the licensee is forfeited. [s. 14(a)]

II. Licence or Registration Requirements

The Task Force received representation that the word "licence" indicates, to some members of the public, a degree of skill, competence or acceptance that is not warranted by the granting of the licence. The Task Force was persuaded, and therefore recommends, that the terminology should be "registered" rather than "licensed". This terminology is used throughout this chapter.

The registration which the Task Force is recommending is not based on competence or expertise. The Task Force is not recommending limiting entry into the construction industry or the oil and gas industry on those grounds. The Task Force, however, believes that registration is virtually an automatic consequence once contractors and subcontractors are required to be fiduciaries with respect to trust funds.

In the absence of a statutory trust, only a contractual relationship exists between the owner, the contractor, subcontractors and material suppliers. Money that is paid to any particular person in the pyramid does not belong to anyone else. In such a case, there is merely a debtor-creditor relationship which can only be enforced through the judicial process. In the case of a debtor corporation which has become insolvent, there is no effective remedy.

The trust provisions which the Task Force is recommending make the relationship substantially different. They transform funds received by the contractor and subcontractors into trust funds. This means that, although a person may have possession of the funds and legal title to them, the beneficial interest vests in those to whom he owes money with respect to the improvement. A corporate trustee is liable if in breach of trust, and so are its directors and officers to the extent that they participated or acquiesced in the breach of trust.

The Task Force unanimously recommends that all contractors and subcontractors in both the construction industry and the energy industry who, in the normal course of business, are in receipt of trust funds should be registered on an annual basis. The Task Force also recommends that these contractors and subcontractors be required to post a $25,000 bond to support and guarantee the obligations imposed by the proposed legislation.

The Task Force further recommends that, in order to obtain registration, a relatively simple test be required of each contractor and subcontractor demonstrating an understanding of the trust obligations, an elementary knowledge of the Builders' Lien Act and a level of accounting necessary to comply with the Act. As well, it must be shown that a separate consolidated trust account is in place.

III. Exemption from the Registration Requirement

The Task Force recommends that those contractors and subcontractors who, in the normal course of business, do not deal with trust funds should not be required to obtain registration since the logic for registration relates to the introduction of trust obligations. For example, contractors who do not have subcontractors and who pay for supplies prior to receiving funds from the owner will be exempt from the registration requirements.

IV. Administration

Although bureaucratic arrangements exist at the present time which could accommodate the registration being proposed in this report, the Task Force recommends that legislation establish an "Industry Committee" which would allow the industry to administer all registration requirements, including forfeiture of bonds. The "Industry Committee" could also develop and administer any tests required of an applicant for registration and could thereafter issue the registration certificate. The costs involved in administering this registration scheme could be recovered from registration fees.

It is envisaged that the "Industry Committee" would be representative of all elements of the construction and energy industries much in the same manner as the Task Force. The "Industry Committee" could establish subcommittees and delegate functions to those subcommittees. For instance, it may be desirable to have separate subcommittees for the energy sector, the large commercial construction sector and the small commercial and residential construction sector. The Task Force recommends that such delegation of authority be permitted in the legislation establishing the proposed "Industry Committee".

Although some discretion should be left with the "Industry Committee" or subcommittees, as the case may be, the Task Force recommends that only a conviction for breach of trust or, in some cases, a civil judgment for breach of trust, could lead to a revocation or non-renewal of a person's registration. The person would have had to be dishonest or reckless with respect to his obligations under the Act before his registration would be revoked or not renewed. It is possible for a person to be in breach of trust and civilly liable for reasons other than dishonesty or reckless disregard of his obligations.

Since a bond is a requirement for obtaining registration, the inability to obtain a bond or to renew it will also result in a person's registration being revoked or not renewed.

With respect to the bond, it is the view of the Task Force that a claim against it could only be made if a person had obtained a judgment for breach of trust. Since it is possible for a plaintiff to obtain a judgment against the defendant trustee for an amount greater than the trustee's trust obligations in a breach of contract action, it should be noted that only to the extent that the defendant is in breach of trust could the bond be called upon. It is further envisaged that the bond would be payable to the "Industry Committee" in the first instance.

In order to discourage contractors and subcontractors from operating without registration, the Task Force recommends that a contractor or subcontractor may only sue on his contract if he holds a valid and subsisting registration certificate. This is a very forceful method of regulation and is found in section 24 of the Real Estate Agents' Licensing Act which provides as follows:

> "(1) No action shall be brought for commission or for remuneration for services in connection with a trade in real estate unless at the time of rendering the services the person bringing the action was licensed as an agent or exempt from the licensing provisions of this Act.
>
> (2) The court may stay an action referred to in subsection (1) at any time on summary application."

The Task Force also recommends that a contractor or subcontractor may only take advantage of the remedies provided by the lien and trust provisions of the proposed legislation if he holds a valid and subsisting registration certificate.

V. Conclusion

The Task Force views the registration recommendation as one of the cornerstones of its report. In order for the scheme of the proposed legislation to provide greater assurance of payment in the construction and oil and gas industries, the trust provisions must be effective. To be effective, they must be understood and adhered to. The trust provisions create a totally different concept and duty of honesty and responsibility in the construction and oil and gas industries. It is extremely important that all elements of these industries understand this significant change.

Honest and responsible contractors and subcontractors will comply with the trust obligations. The dishonest ones should not be handling trust funds and should not be in the industry. Only registration will ensure this result.

Chapter 8: Labourers under the Builders' Lien Act

I. Introduction

Under the current legislation, a "labourer" is defined to mean "a person employed for wages in any kind of labour whether employed under a contract of service or not". A labourer who works on improving the owner's land has a lien for unpaid wages on the owner's estate or interest in that land.

The new Employment Standards Code, S.A. 1988, c. E-10.2 imposes a trust obligation on every employer in the following terms:

> 110(1) Notwithstanding any other Act, every employer shall be deemed to hold all wages, overtime pay, vacation pay and general holiday pay accruing due or due to an employee in trust for the employee, whether or not the amount accruing due or due has in fact been kept separate and apart by the employer.
>
> (2) Subject to subsection (3) and section 111, wages, overtime pay, vacation pay and general holiday pay accruing due or due to an employee shall be deemed to be a secured charge on the property and assets of the employer to a maximum of $7,500 and payable in priority to any other claim or right in the property or assets including
>
> (a) any claim or right of the Crown in right of Alberta, including, without limitation, claims or rights of the Workers' Compensation Board, and
> (b) any lien, charge, encumbrance, mortgage, assignment, including an assignment of book debts, debenture or other security of whatever kind of any person...

Given the requirement of a separate trust account for those in the construction and energy industries, it is quite probable that the funds in those trust accounts will not be considered money over which an employer has control or beneficial ownership and thus will not be subject to claims by employees, other than those involved on the project. It would appear, therefore, that any trust funds under the Task Force's proposals would not be money impressed with the trust for the benefit of an employee generally, unless such money ceased to be trust funds.

However, in order for there to be no question of the relationship between the Employment Standards Code and the proposed trust conditions under the Builders' Lien Act, the Task Force recommends a consequential amendment to the Employment Standards Code in order to make it clear that the pool of money which is impressed with the trust under the Employment Standards Code is not the same pool of money which is subject to a trust under the Builders' Lien Act.

Therefore, it appears to the Task Force that a construction employee can be given the same lien rights as a contractor, subcontractor or supplier, without the Employment Standards Code and the Task Force's trust proposals coming into conflict. That is, a construction employee may be given the same right to lien as he has today with the same priorities and, in addition, may become a beneficiary in the trust chain.

II. Wages

While the Task Force does not recommend any change in the present ability of labourers to register a lien for wages, it does recommend a change in the definition of "wages".

Under current builders' lien legislation in Alberta, "wages" do not include the fringe benefits that make up a significant portion of an employee's entitlement. Both Ontario and Saskatchewan have expanded the definition of wages under their lien legislation. In Ontario, "wages" is defined to mean

> "the money earned by a worker for work done by time or as piece work, and includes all monetary supplementary benefits, whether provided for by statute, contract or collective bargaining agreement".

In Saskatchewan, "wages" is defined to mean

> "remuneration or compensation of any kind of a person employed as a labourer whether by time, or as piece work or otherwise and includes:
>
> (i) salary, pay or commission;
> (ii) remuneration in respect of overtime;
> (iii) statutory holiday pay;
> (iv) money required to be paid to an employee under The Labour Standards Act; and
> (v) all supplementary benefits whether provided for by statute, contract or collective bargaining agreement."

Referring to fringe benefits, the Saskatchewan Report stated that "these items are just as much part of the employment package" (at page 227), a comment with which the Task Force agrees.

The Task Force recommends that the definition of "wages" should include all fringe benefits which the employer had been paying on behalf of the employee.

III. Priority of Wages

The current Builders' Lien Act provides that a lien for the wages of a labourer has priority to the extent of six weeks' wages. The legislation also provides that, as among themselves, labourers share equally. The Task Force is of the view that the priority for six weeks' wages should be retained in a lien action.

The Task Force recommends, however, that this priority should not apply to any distribution of trust funds, since such a priority at one level of the construction pyramid could work to the detriment of trust beneficiaries, including labourers, at other levels.

IV. Assignment of Rights

The current legislation provides that the "right of a lienholder may be assigned in writing". Case law has held that the assignment in writing must be obtained before registration of the lien. In many instances, however, this may be impossible. While the Task Force agrees that a person or corporate body must have a verbal assignment before a lien is registered or a Stop Notice is served, there is no reason why the assignment in writing must have been obtained at such time. It would seem reasonable that the assignment in writing need not be obtained until a notice to prove lien or Stop Notice could be served. Therefore, the Task Force recommends that the current legislation should be amended to reflect the following principles:

1. The rights of a lienholder may be assigned;
2. The assignment must be obtained verbally prior to the registration of a lien or service of a Stop Notice; and
3. The assignment must be evidenced in writing not later than 15 days after registration of the lien or service of the Stop Notice.

Chapter 9: Liens Against the Crown

At the present time, the Crown is not bound by the Builders' Lien Act: see, Interpretation Act, R.S.A. 1980, c. I-7, s. 14. That is, the lands of the Crown are not lienable. Rather, the payment of public works creditors is dealt with in sections 13 to 19 of the Public Works Act, R.S.A. 1980, c. P-38.

The suggestion has been made by the industry that these sections of the Public Works Act should be repealed and that the Crown should be bound by the Builders' Lien Act. The argument is made that it is unreasonable to expect subcontractors and suppliers to be able to determine whether or not they are dealing with a situation under the Public Works Act or one covered by the Builders' Lien Act. First, it is not always clear whether or not one is dealing with the Crown. Second, because of the difference in time periods involved, that initial question is extremely important and should one guess wrongly, one might well find that the relevant time period has gone by.

Most other jurisdictions in Canada make the Crown subject to their builders' lien legislation. In Ontario, for example, an owner is defined to mean "any person, including the Crown...". [s. 1(1)(15)]. Section 3(1) of Ontario's Construction Lien Act provides that "this Act binds the Crown...". Section 16 provides the usual caveat to the Crown's being bound by builders' lien legislation, namely, that the "lien does not attach to the interests of the Crown in a premises." [s. 16(1)]

In Saskatchewan, section 26(1) of The Builders' Lien Act provides that a "lien does not attach to and cannot be registered against the estate or interest in land of the Crown." Subsection (3) provides that where the Crown is an owner, the lien does not attach to the land but constitutes a charge on the holdback required to be retained under the Act as well as being a charge upon

> "any additional amount owed in relation to the improvement by a payer to the contractor or to any subcontractor whose contract or subcontract was in whole or in part performed by the provision of services or materials giving rise to the lien."

The Task Force was unanimous in its recommendation to bring the Crown into the Builders' Lien Act regime, thus removing it from the ministerial discretion that now exists under the Public Works Act. Although a lien cannot be registered against Crown land, a Stop Notice could be served on the Crown which would place an obligation on the Crown to withhold the amount claimed in the Stop Notice from the withhold the amount claimed in the Stop Notice from the general contractor. As well, funds paid by the Crown to the general contractor would be trust money to which the trust obligations of the proposed legislation will apply.

Chapter 10: Summary of Recommendations

CHAPTER 1: INTRODUCTION

The Joint Government/Industry Task Force on Builders' Liens was established by the Attorney General and consists of representatives nominated by a number of associations which have a direct interest in the Builders' Lien Act.

Since lien rights are an historically accepted part of the construction and energy industries in every common law province as well as in virtually every state of the United States, the Task Force was unanimous in its view not to recommend repeal of the Builders' Lien Act.

Early in its deliberations, the Task Force resolved that the primary objective of its proposals would be to create a legislative framework which would provide greater assurance that everyone in the construction and energy industries would be paid. The recommendations therefore go beyond mere lien rights.

The Task Force found the California lien system appealing in a number of aspects. In many respects, large projects in Canada are now conducted in much the same manner as the California system. In California, the use of statutorily prescribed "lien waiver forms" is an integral part of its system. It is, in nature, more of a receipt than a lien waiver. The Task Force is recommending that statutory forms be provided that will serve as evidence of a payment receipt, such that an owner can be assured that there will be no liens arising as a result of work for which a receipt has been issued.

The recommendations of this report should be viewed as a whole. The removal of any one of the major elements of those recommendations would significantly hamper the achievement of the Task Force's objectives.

CHAPTER 2: THE STATUTORY TRUST

1. Comprehensive Trust Provisions

The Task Force recommends that Alberta should have comprehensive trust provisions similar to those now in existence in Ontario and Saskatchewan. Initially, a trust obligation should exist only where a contractual relationship exists. However, a Stop Notice (a new remedy) served on the owner by a subcontractor or supplier would create an additional trust obligation on the owner in favour of the person serving the Stop Notice for the amount claimed in it.

2. Trust Funds of the Owner

The Task Force recommends that the following funds in the hands of the owner should constitute trust funds:

(a) Funds secured by a mortgage, or other security, advanced to the owner for the purpose of financing the improvement;

(b) Any funds in the hands of the owner, or received by the owner, for payment of the improvement;

(c) Any funds, or source of funds, identified by the owner to the contractor as being funds earmarked for paying the cost of the improvement;

(d) Any revenue generated from the improved land, subject to prior encumbrances;

(e) Any funds derived from a sale of the improvement, subject to normal expenses and prior encumbrances; and

(f) Net proceeds of insurance should the improvement be damaged or destroyed.

3. Trust Funds of the Contractor or Subcontractor

The Task Force recommends that funds received by the contractor and subcontractors on account of the contract price should constitute trust funds to the extent that debts are owing to other subcontractors and suppliers with respect to the project, subject to the right of set off arising out of the project. If funds have been advanced by the contractor or subcontractor out of his own funds or borrowed and paid to beneficiaries, he may repay himself, or the lender, that amount from funds which would otherwise be trust funds.

4. Consolidated Trust Account

The Task Force recommends that all contractors and subcontractors who are in receipt of trust funds should be required to deposit such funds in a separate consolidated trust account maintained in Alberta. Owners, however, should not be required to maintain a separate trust account.

5. Trustee Can Repay Funds Borrowed to Pay Beneficiaries

The Task Force recommends that if contractors and subcontractors used their own funds or borrowed funds to pay trust obligations, the sum equal to that paid to trust beneficiaries should not constitute trust funds.

6. Right to a Trust Claim

The Task Force recommends that a person must have been entitled to a lien in order to have a trust claim.

7. Separate Remedy for Trust Funds

The Task Force recommends that the remedy to pursue trust funds should be the Stop Notice, and the remedy to pursue claims against the land should continue to be the Lien. Each remedy could be pursued independently or both could be pursued together.

8. Trust Duties Terminate Upon Payment

The Task Force recommends that trust duties should terminate upon payment of all trust funds to beneficiaries. If a person has underbid a project, he will receive less trust funds than he has obligations. Nevertheless, he will discharge his trust duties if he pays out the trust funds received.

9. Setoff of Counterclaim Arising Out of Project

The Task Force recommends that a trustee should be able to set off against trust funds any counterclaim against a beneficiary which arises out of the project.

10. Sanction for Breach of Trust

The Task Force recommends that a provincial offence for breach of trust should be created and that directors and officers should be subject to the offence provisions if they participated or acquiesced in a corporate decision to breach a trust duty. It is also recommended that fines should be significant in order to create a strong deterrent.

11. Personal Liability

The Task Force recommends that the legislation should expressly pierce the corporate veil and should create personal civil liability for directors and officers who participated or acquiesced in a corporate breach of trust.

CHAPTER 3: THE STOP NOTICE

1. Separation of Lien Remedy from Trust Remedy

The Task Force recommends that the remedy to encumber the land, the lien, and the remedy to pursue trust funds, the Stop Notice, be separated. Each remedy could be pursued independently or both could be pursued simultaneously.

2. Framework of the Stop Notice

The framework of the proposed Stop Notice can be summarized as follows:

(a) The Stop Notice will be a document prescribed by regulation;

(b) The Stop Notice will be effected by service on the owner and not by registration against the owner's land title;

(c) An unpaid beneficiary, other than a contractor, may serve a Stop Notice on the owner. This will create a new trust relationship between the owner and the person serving the Stop Notice. A contractor need not serve a Stop Notice since trust obligations already exist between him and the owner;

(d) The unpaid beneficiary will have 90 days from completion of his contract to serve the Stop Notice;

(e) Where the owner is served with a Stop Notice by a subcontractor or supplier, he will become a trustee for the person serving the Stop Notice to the extent of the amount claimed in it. The obligation of the owner, when served with a Stop Notice, will be to set aside the amount claimed in it to the extent that trust funds are in his hands, or when trust funds come into his hands in the future;

(f) The owner must, within 10 days of being served with a Stop Notice, serve an Answer, in prescribed form, on the unpaid beneficiary advising that:

(i) trust money has been set aside;
(ii) although trust money has not been set aside, it will be set aside from a source which constitutes trust money; or
(iii) no money has been set aside and the reason for not doing so;

(g) If the unpaid beneficiary who served the Stop Notice wishes the money to be paid into court, he must commence an action against his immediate trustee. The owner will be served with a copy of the Statement of Claim and will then have to pay the money previously set aside into court to the credit of the action;

(h) If the unpaid beneficiary who served the Stop Notice does not commence an action against his trustee within 120 days of serving the Stop Notice on the owner, the Stop Notice lapses and the owner may pay the amount set aside to the contractor without jeopardy;

(i) Where an owner is served with a Stop Notice, or has trust obligations to the contractor, and is insolvent, the person who served the Stop Notice, or the contractor, as the case may be, may appoint a receiver to collect the revenue generated by the improvement or other money which constitutes trust money;

(j) The service of a Stop Notice, unlike the registration of a lien, will not affect mortgage priorities and should therefore not interrupt the flow of mortgage financing.

3. Stop Notice Creates a Trust Obligation

The service of a Stop Notice on the owner will create a trust duty between the owner and the person serving the Stop Notice which would not otherwise exist.

4. Stop Notice Does Not Encumber Land

The Stop Notice does not encumber the land and therefore does not affect priorities or encumbrances against the land. It is expected that if subcontractors and suppliers consider the owner solvent, they would use the Stop Notice instead of the lien. Further, the strong adverse reaction to the use of the lien by a subcontractor or supplier should not be encountered with the use of the Stop Notice.

CHAPTER 4: ELIMINATION OF THE STATUTORY HOLDBACK

The Task Force recommends that the statutory requirement of a holdback should be eliminated, although it is anticipated that contractual holdbacks may then occur. The purpose of this recommendation is to help speed up the flow of funds. It will, as well, significantly simplify the legislation.

After considerable representations and analysis, the Task Force concluded that the holdback, being a notional concept, is, in most cases, not very valuable security. In its view, elimination of the statutory holdback will result in an increased flow of funding which, when combined with the comprehensive trust provisions and the Stop Notice, will provide superior security and greater assurance of payment for subcontractors and suppliers. Lastly, elimination of the statutory holdback should encourage better business practices, such as proper credit checks and formal contractual relationships.

CHAPTER 5: OIL AND GAS

1. Operator: Same Trust Obligations as Owner

The Task Force recommends that the trust obligations of an operator, or a farmee, should be the same as if he were an owner in a construction project.

2. Trust Concept Applicable

The trust provisions applicable to the construction sector should apply to the oil and gas industry.

3. Trust Remedy to be Used

Once minerals or oil and gas are severed from the improved land and sold, the proceeds should become trust funds and would be subject to enforcement through the trust remedy rather than through the lien.

4. Lien Period Extended

The Task Force recommends that the lien period in the oil and gas industry should be extended from 45 days to 90 days.

5. "Land" Broadly Interpreted

Revenue derived from the "land" improved should constitute trust funds. The term "land" should mean that interest held by an owner in the one lease or licence. It follows that, if the lease or licence includes producing wells, the owner's trust will include the revenue generated by those other wells, provided that the interest is held by the same owner.

CHAPTER 6: APPOINTMENT OF A RECEIVER

The Task Force recommends that an unpaid beneficiary should be able to apply to the court for the appointment of a receiver to receive trust funds, in addition to the existing rights to the appointment of a receiver pursuant to the lien provisions.

CHAPTER 7: LICENSING OR REGISTRATION

1. Requirement for Registration

The Task Force recommends that all contractors and subcontractors in both the construction industry and the oil and gas industry should be registered on an annual basis and should be required to post a $25,000 bond to support and guarantee the obligations imposed by the proposed legislation.

The Task Force recommends that in order to obtain registration, an applicant must:

(a) have a separate consolidated trust account;

(b) obtain and provide a bond; and

(c) pass a relatively simple test demonstrating an understanding of trust obligations, an elementary knowledge of the Builders' Lien Act and a level of accounting necessary to comply with the legislation.

2. Registration Not Based on Competence

The Task Force recommends that registration should not be based on competence or experience.

3. Individual Must be Registered as well as Corporation

The Task Force recommends that, with respect to a corporate contractor or subcontractor, both the company and at least one individual who is an officer or director of the company must be registered.

4. Exemption from Registration

The Task Force recommends that those contractors and subcontractors who, in the normal course of business, do not deal with trust funds should not be required to obtain registration.

5. Administration by Industry

The Task Force recommends that legislation should establish a representative "Industry Committee" to administer all registration requirements and tests, including the forfeiture of bonds. The legislation should also permit the "Industry Committee" to delegate authority to industry subcommittees.

6. Forfeiture Only After Judgment

The Task Force recommends that a bond should only be forfeited if a judgment of a court finds a breach of trust.

7. Revocation of Registration Possible

The Task Force recommends that registration may be revoked or not renewed if a contractor or subcontractor does not maintain a consolidated trust account as required or if in breach of trust.

CHAPTER 8: LABOURERS UNDER THE BUILDERS' LIEN ACT

1. Employees to Maintain Rights

Although the new Employment Standards Code creates an employer trust for unpaid wages, the Task Force recommends that employees in the construction and energy industries continue to have lien rights and derive the benefit of the new trust regime proposed for the construction and energy industries.

2. Definition of "Wages" Expanded

The Task Force recommends that the definition of "wages" for purposes of the proposed lien legislation be expanded to include fringe benefits since they are as much a part of remuneration as are direct wages.

3. Assignment of Rights

The Task Force recommends that any assignment of lien rights or trust claims be permitted verbally initially and that such assignment must be evidenced in writing within 15 days of registering the lien or serving the Stop Notice.

CHAPTER 9: LIENS AGAINST THE CROWN

The Task Force recommends that the Crown should be bound by the Builders' Lien Act. Although a lien could not be registered against Crown land, nor would the Crown be a trustee, nevertheless, a Stop Notice could be served on the Crown which would place an obligation on the Crown to withhold the amount claimed in the Stop Notice from the general contractor.

SCHEDULE "A"

JOINT GOVERNMENT/INDUSTRY TASK FORCE ON BUILDERS' LIENS

Chairman

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Building Owners and Managers Association
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Canadian Association of Oilwell Drilling Contractors
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SCHEDULE "B"

Legislative History of the Builders' Lien Act

1. (1906) 1906 c. 21 An Act for the Benefit of Mechanics and Labourers
2. (1907) 1907 c. 5 s. 17 An Act to Amend the Statute Law
3. (1908) 1908 c. 20 s. 12 An Act to Amend the Statute Law
4. (1909) 1909 c. 4 s. 10 An Act to Amend the Statute Law
5. (1915) 1915 c. 2 s. 27 An Act to Amend the Statute Law
6. (1916) 1916 c. 3 s. 19 An Act to Amend the Statute Law
7. (1922) 1922 c. 4 s. 29 An Act to Amend the Statute Law
8. (1922) R.S.A. 1922, c. 182 An Act for the Benefit of Mechanics and Labourers
9. (1930) 1930 c. 7 An Act Respecting the Liens of Mechanics, Wage-earners and others
10. (1931) 1931 c. 24 An Act to Amend the Mechanics' Lien Act, 1930
11. (1942) R.S.A. 1942, c. 236 An Act Respecting Liens of Mechanics, Wage-earners and others
12. (1943) 1943 c. 31 An Act to Amend the Mechanics' Lien Act
13. (1946) 1946 c. 56 An Act to Amend the Mechanics' Lien Act
14. (1947) 1947 c. 64 An Act to Amend the Mechanics' Lien Act
15. (1948) 1948 c. 65 An Act to Amend the Mechanics' Lien Act
16. (1949) 1949 c. 64 An Act to Amend the Mechanics' Lien Act
17. (1952) 1952 c. 51 An Act to Amend the Mechanics' Lien Act
18. (1953) 1953 c. 72 An Act to Amend the Mechanics' Lien Act
19. (1955) R.S.A. 1955, c. 197 An Act Respecting Liens of Mechanics, Wage-earners and others
20. (1960) 1960 c. 63 An Act to Amend the Mechanics' Lien Act
21. (1960) 1960 c. 64 An Act Respecting Liens of Mechanics, Material Suppliers, Wage-earners and others
22. (1963) 1963 c. 34 An Act to Amend the Mechanics' Lien Act
23. (1970) 1970 c. 14 An Act Respecting Liens of Builders, Material Suppliers, Wage-earners and others
24. (1970) R.S.A. 1970, c. 35 The Builders' Lien Act
25. (1975) 1975 (2nd) c. 10 s. 11(2) The Department of Energy and Natural Resources Act
26. (1978) 1978 c. 50 s. 22 The Court of Appeal Act
27. (1978) 1978 c. 51 s. 38(4) The Court of Queen's Bench Act
28. (1980) R.S.A. 1980, c. B-12 The Builders' Lien Act
29. (1985) S.A. 1985, c. 14 The Builders' Lien Amendment Act, 1985
30. (1986) S.A. 1986, c. D-18.1, s. 14 The Department of Energy Act